

DIRECTORATE-GENERAL FOR INTERNAL POLICIES

POLICY DEPARTMENT **D**
BUDGETARY AFFAIRS

Budgets

Budgetary Control



The implications of EIB and EBRD co-financing for the EU budget

STUDY



DIRECTORATE GENERAL FOR INTERNAL POLICIES
POLICY DEPARTMENT D: BUDGETARY AFFAIRS

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This document was requested by the European Parliament's Committee on Budgets. It designated Ivailo Kalfin and Jean-Luc Dehaene, MEPs, to follow the study.

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DIRECTORATE GENERAL FOR INTERNAL POLICIES
POLICY DEPARTMENT D: BUDGETARY AFFAIRS

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STUDY

Abstract

Recent years have seen the growth of a number of EU co-financing instruments designed to enhance the leverage of the EU budget by working more closely with the European Investment Bank and the European Bank for Reconstruction and Development. However, the growth of such instruments raises potential concerns in relation to financial control and liability, in relation to governance, transparency and visibility and in relation to the extent to which such activity helps the deliverability of EU objectives.

22/03/2011

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LIST OF ABBREVIATIONS

- ACP** African, Caribbean and Pacific
- BFI** Bilateral Financial Instrument
- CEB** Council of Europe Development Bank
- CIP** Competitiveness and Innovation Framework Programme
- EBRD** European Bank for Reconstruction and Development
- EDF** European Development Fund
- EE** Energy Efficiency
- EIB** European Investment Bank
- EIF** European Investment Fund
- ELENA** European Local Energy Assistance
- ERDF** European Regional Development Fund
- EP** European Parliament
- ESF** European Social Fund
- EU** European Union
- EWBJF** European Western Balkans Joint Fund
- FEMIP** Facility for Euro-Mediterranean Investment and Partnership
- GIF** Growth and Innovation Facility
- HF** Holding Fund
- HIPC** Heavily-Indebted, Poor Countries
- ICT** Information and Communication Technology
- IFI** International Financial Institution
- ITF** Infrastructure Trust Fund

- JASMINE** Joint Action to Support Micro Finance Institutions in Europe
- JASPERS** Joint Assistance to Support Projects in European Regions
- JEREMIE** Joint European Resources for Micro to Medium to Medium Enterprises
- JESSICA** Joint European Support for Sustainable Investment in City Areas
- KfW** Kreditanstalt für Wiederaufbau
- LGB** Loan-Grant Blending
- LGI** Loan Guarantee Instrument
- LGTT** Loan Guarantee Instrument for TENs Transport
- MA** Managing Authority
- MFI** Microfinance Institution
- NIF** Neighbourhood Investment Facility
- PFG** Project Financiers Group
- PPP** Public-Private Partnership
- RES** Renewable Energy Source
- RSFF** Risk Sharing Finance Facility
- SBF** Stand-by Credit Facility
- SME** Small and Medium-Sized Enterprise
- SMEG** Small and Medium-Sized Enterprise Guarantee Facility
- TA** Technical Assistance
- TENs** Trans-European Networks
- TEN-T** Trans-European Networks (Transport)
- UDF** Urban Development Fund
- WBIF** Western Balkans Investment Framework

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EXECUTIVE SUMMARY

This study has been prepared during December 2010 to February 2011 for the European Parliament's Committee on Budgets, and focuses on the implications from the growth of co-financing for the EU budget with particular focus on links with the European Investment Bank (EIB) and European Bank for Reconstruction and Development (EBRD).

As part of the deliberations over the Financial Framework 2007-13, the EU institutions reached agreement on the development of co-financing instruments with the aim of reinforcing the leverage effect of the European Union budget in order to increase the EU's capacity to deliver on its strategic objectives.

In response to this, there has been a growth of co-financing in which funds from the EU budget works alongside loans from the EIB and EBRD with the objective of leveraging greater financial outcomes than would otherwise be possible. However, such activity raises three particular concerns which are central to this study: in relation to financial control and liability; in relation to governance, in particular to issues of transparency and visibility, and in relation to the extent to which such activity helps the deliverability of EU objectives.

In order to explore these issues, the study combines desk-based documentary analysis with exploratory interviews which have been conducted with over 50 key stakeholders and policy makers from the EIB, EBRD, European Commission and European Court of Auditors.

The key questions raised, and conclusions drawn, from this research are as follows:

- **Budgetary Liability:** Central to the study is the question of whether the growth of co-financing raises threats to the budget in terms of budgetary liability. Does working with the EIB and EBRD subject the EU budget to particular threats in the event, for example, of losses by one or other of the Banks?

Overall, we find that there are in fact few, if any, concerns in a formal sense in terms of budgetary liability. All of the co-financed instruments involve allocations to programmes which are capped in size and so none of these instruments pose a risk to the budget beyond that which is initially committed. Even in those cases in which the financial instrument involves a form of guarantee there remains no liability beyond that which was originally committed during the design of the instruments.

- **The External Mandate:** At present much external lending by the EIB is undertaken on the basis of a budgetary guarantee which underpins EU external policies covering sovereign and political risks. A central question for this study is whether the provision within the external mandate is sufficient given the present lending volumes of the EIB and whether it poses any threats to the EU budget.

Overall, we find here in agreement with earlier evaluations which have been undertaken of the guarantee fund, namely that it is effectively managed, appropriately provisioned, has strong governance mechanisms in place and poses little, if any, theoretical or practical risks to the budget. However we acknowledge that this may change if the EIB were to significantly increase its external lending activity, assuming that this were not taken at the bank's own risk.

- **Budgetary Management:** The report considers any possible threat to budgetary discipline with specific reference to (a) EU guarantees provided for loans to member states and (b) guarantees provided to the EIB for external activities. This required us to examine the two alternative approaches to loss provisioning employed by the EU. In the case of EU guarantees for loans to member states, provisioning is provided through headroom in the EU budget. A dedicated reserve fund (the Community Guarantee Fund) provisions for losses specifically arising from the EU guarantee extended to the EIB for its external lending activities.

Our conclusions are that both approaches to loss provisioning are valid. Although they 'operate' differently, in their own ways they both provide adequate protection for the EU budget through sufficient, perhaps over-, provisioning. Evaluations of both approaches (and external evaluation of the Community Guarantee Fund and an internal evaluation of headroom within the EU budget) simulated harsh default scenarios - well beyond those which might be likely to crystallise - and under all tested scenarios the provisioning mechanisms and amounts were found to be more than adequate. All decisions in relation to member state loans and EIB external activity were made with the full knowledge and approval of the Budgetary Authority and strict, agreed limits on operations had been established (e.g. limits on EIB lending volumes).

- **Budgetary Control:** A key question is whether the mechanisms which are presently in place are sufficient for the EP to exert budgetary control. Of central importance is whether or not the EP can control and/or influence programmes which are only part funded by the EU budget.

Our conclusions are that while the EP is formally involved in the framing of these instruments, and in the decision to place parts of the budget at the disposal of financial intermediaries, so maintaining levels of control in the formal sense, a number of challenges present themselves in terms of the arms-length nature of that control following the implementation of co-financing. In particular, control is clearly reduced in a theoretical sense in a framework in which a financial instrument is run via an intermediary (such as the EIB or EBRD) who then passes management of financial disbursement to a further intermediary (such as a bank).

- **Relationship between Co-financing and the Strategic Objectives of the EU:** Of central concern here is whether working with financial intermediaries serves to skew the priorities of the Union. Bank loans, after all require a borrower, raising the question of whether their interests are compatible with those of the EU.

Overall, we find mixed conclusions here. On the positive side, there is clear evidence that co-financing has been undertaken in areas which have seen considerable success in delivering EU policy priorities, such as innovation, research and competitiveness – all of which are fundamental strategic objectives of the EU. However, there has been considerable variation in the capacity of the 'new' member states and the SME sectors to benefit from these instruments, leading to concerns that, at present, co-financing may be best suited to those markets which are relatively developed. This is particularly demonstrated with the ongoing and severe problems caused by both the financial crisis and the low levels of absorption of the structural funds in many of these states – problems which it is perhaps unrealistic to expect co-financing to overcome.

- **Governance and Transparency:** Co-financing opens up concerns that the associated policy instruments will be increasingly complicated, so reducing questions of political control, governance and accountability. A desire to explore such concerns are central to this study.

Here we conclude that there are two particular aspects to the transparency issue. The first is that co-financing simply makes it more difficult for the EU institutions themselves to track how the budget is spent and to evaluate the effectiveness of that spending. The second relates to the tensions which exists at the heart of co-financing with the EIB and EBRD, in particular, in terms of the EU's desire for transparency and openness alongside the EIB's and EBRD's desire to respect their commercial confidentiality, which are central to their lending activity. Such tensions are very difficult to ameliorate as they are at the heart of the adoption of co-financing.

- **Visibility:** Given that co-financing involves multiple partners, in what may appear to be increasingly complex policy instruments, there may also be implications for the visibility of the Union with beneficiaries and stakeholders. We also explore how co-financing affects visibility within the EU as a whole.

Our conclusions are that, in a context in which visibility of many EU schemes is low, co-financing poses particularly acute problems in terms of visibility. Overall, in spite of the fact that there has been a consistent pattern in which the EU has attempted to develop a number of schemes designed to enhance visibility, our findings points to a pattern of low stakeholder and beneficiary awareness across the board. At a theoretical level this is hardly surprising – co-financing frequently works through intermediaries who are ultimately responsible for disbursing the funds, so making the EU's role increasingly opaque. Yet there are also acute problems for visibility between the EU institutions themselves, with low levels of understanding of the unique natures of the EIB and EBRD and a general lack of awareness of the scope and scale of co-financing.

As this report focuses on two key European banks (the EIB and the EBRD) a summary table follows that provides a high-level 'at a glance' comparison of these two institutions.

Table 1: EIB/EBRD at a Glance

	EIB	EBRD
Established	1958	1991
Credit Rating	AAA/Aaa	AAA/Aaa
Objective	The Treaty-based European Union's long-term lending institution. A policy-driven bank supporting EU priority objectives, notably – inside the EU, cohesion, competitiveness, environment, TENs, energy and SMEs – and, outside the EU, technical and economic co-operation with third countries and development through financing operations in the public and private sectors.	To promote the economic progress of CEE countries through close and coordinated cooperation. To help their economies become more internationally competitive and assist them in their reconstruction and development. To foster the transition towards market-oriented economies and provide for private investment.
Headquarters	Luxembourg	London
No of Regional Offices	23 (11 outside the EU)	35
No of Employees (end-2009)	1,906 (EIB Group)	1,492
% Employees at HQ	92%	76%
Shareholders	27 Member States of the EU	61 Countries (including all EU Member States), the EC and the EIB
Main Shareholdings	France, Germany, Italy and the UK hold 65% of share capital	EC, EC Member States and EIB hold over 60% of share capital
Capital Subscribed	EUR 232 billion	EUR 33 billion
Countries of Operations	EU + 140 countries worldwide	30 countries from Central Europe and Central Asia
Vol. of Loan Signatures (2010)	EUR 72 billion	EUR 9 billion
Investment Focus	Public & private sectors	Private sector
Products	Senior loans, mezzanine finance, indirect equity, guarantees & technical assistance	Senior loans, mezzanine finance, equity, guarantees & technical assistance
Average Loan Size	EUR 130 million	EUR 25 million
Project Selection Rationale	-Contribution to EU policy objectives -Quality of underlying investments -Value-added by the EIB -Subsidiarity -Sound banking	-Additionality -Transition impact -Sound banking
Risk Culture	Community guarantee for external lending	Less than 20% of investments have a sovereign guarantee
Pricing	Pricing based on cost-recovery	Pricing is market-based

ZUSAMMENFASSUNG

Diese Studie wurde im Zeitraum Dezember 2010 bis Februar 2011 für den Haushaltsausschuss des Europäischen Parlaments erstellt und hat die Auswirkungen von Kofinanzierungen auf den EU-Haushalt unter besonderer Berücksichtigung von Verbindungen zur Europäischen Investitionsbank (EIB) und zu Europäischen Bank für Wiederaufbau und Entwicklung (EBWE) zum Gegenstand.

Im Zuge der Beratungen über den Finanzrahmen 2007-2013 einigten sich die EU-Organe auf die Entwicklung von Kofinanzierungsinstrumenten mit dem Ziel, die Hebelwirkung der aus dem Haushalt der Europäischen Union bereitgestellten Mittel zu verstärken und so die Möglichkeiten der EU zu verbessern, ihre strategischen Zielsetzungen zu erreichen.

Als Reaktion darauf ist eine Zunahme von Kofinanzierungen zu verzeichnen, bei denen neben EIB- und EBWE-Darlehen Mittel aus dem EU-Haushalt eingesetzt werden, um höhere finanzielle Ergebnisse zu erzielen, als andernfalls möglich wären. Doch ein solches Vorgehen könnte vor allem in drei Bereichen problematisch werden, die in dieser Studie im Mittelpunkt stehen: in Bezug auf die Finanzkontrolle und finanzielle Haftung; in Bezug auf Governance, insbesondere in Fragen der Transparenz und Bekanntheit, sowie in Bezug auf das Ausmaß, in dem eine Aktivität für das Erreichen der Zielsetzungen der EU hilfreich ist.

Zur näheren Betrachtung dieser Punkte wurde für diese Studie die Schreibtischrecherche mit Sondierungsgesprächen mit über 50 wichtigen Vertretern und Entscheidungsträgern von EIB, EBWE, Europäischer Kommission und Europäischem Rechnungshof verbunden.

Die Hauptfragen, die gestellt wurden, und die Schlussfolgerungen, die nach diesen Recherchen gezogen wurden, lauten wie folgt:

- **Haftung des Haushalts:** Im Mittelpunkt der Studie steht die Frage, ob die Zunahme der Kofinanzierungen eine Gefahr für den Haushalt in Form einer Haftung darstellen könnte. Ist die Arbeit mit der EIB und dem EBWE für den EU-Haushalt mit besonderen Risiken verbunden, beispielsweise im Falle von Verlusten bei einer der Banken?

Alles in allem stellen die Verfasser fest, dass die Sorge, formell könne Haftung seitens des Haushalts bestehen, weitgehend unbegründet ist. Alle kofinanzierten Instrumente umfassen Zuteilungen für Programme, deren Umfang begrenzt ist, und so stellt über die ursprünglich gebundenen Beträge hinaus keines dieser Instrumente ein Risiko für den Haushalt dar. Auch in Fällen, in denen das Finanzierungsinstrument mit einer Form von Bürgschaft verbunden ist, besteht keine Haftung über die ursprünglich bei der Konzipierung der Instrumente gebundenen Mittel hinaus.

- **Das Außenmandat:** Gegenwärtig wird ein Großteil der Finanzierungstätigkeit der EIB in Drittländern, die der Unterstützung der EU-Außenpolitik dient, mit einer Haushaltsgarantie besichert, die die staatlichen und politischen Risiken deckt. Eine zentrale Frage in dieser Studie lautet, ob die Bereitstellung im Rahmen des Außenmandats angesichts des aktuellen Darlehensumfangs der EIB ausreichend ist und ob eine Gefahr für den EU-Haushalt besteht.

Insgesamt gesehen stimmen die Verfasser hier mit früheren Bewertungen des Garantiefonds überein, nämlich dass er effektiv verwaltet wird, angemessen ausgestattet ist, über solide Leitungsmechanismen verfügt und theoretisch und praktisch kaum eine Gefahr für den Haushalt darstellt. Sie räumen allerdings ein, dass sich dies ändern kann, wenn die EIB ihre Tätigkeit in Drittländern deutlich verstärken müsste, sofern sie dies nicht auf eigenes Risiko tut.

- **Haushaltsführung:** Im Bericht werden alle denkbaren Bedrohungen für die Haushaltsdisziplin unter besonderer Berücksichtigung der a) EU-Garantien für Darlehen an Mitgliedstaaten und b) Garantien für die Tätigkeit der EIB in Drittländern untersucht. Dafür waren die beiden alternativen Verfahrensweisen für Rückstellungen bei Verlusten zu prüfen, die die EU anwendet. Bei EU-Garantien für Darlehen an Mitgliedstaaten ist durch Spielraum im EU-Haushaltsplan vorgesorgt. Ein spezieller Rückstellungsfonds (der Garantiefonds der Gemeinschaft) sorgt eigens für Verluste vor, die sich aus der EU-Garantie für die Finanzierungstätigkeit des EIB in Drittländern ergeben könnten.

Die Verfasser gelangen zu dem Schluss, dass beide Verfahrensweisen für Rückstellungen bei Verlusten ihre Berechtigung haben. Zwar „funktionieren“ sie unterschiedlich, bieten aber beide auf ihre Weise durch ausreichende, vielleicht sogar zu hohe Rückstellungen einen angemessenen Schutz für den EU-Haushalt. Bei Evaluierungen beider Ansätze (und einer externen Bewertung des Garantiefonds der Gemeinschaft und einer internen Bewertung des Spielraums im EU-Haushalt) wurden extreme Standardszenarien simuliert - die weit über das hinaus gingen, was eintreten könnte -, doch bei allen untersuchten Szenarien erwiesen sich die Vorsorgemechanismen und -beträge als mehr als ausreichend. Alle Entscheidungen zu Darlehen an Mitgliedstaaten und zur Tätigkeit der EIB in Drittländern wurden mit voller Kenntnis und Zustimmung der Haushaltsbehörde getroffen, und die Maßnahmen unterlagen strengen, abgestimmten Beschränkungen (z. B. Obergrenzen für den Umfang von EIB-Darlehen).

- **Haushaltskontrolle:** Eine wichtige Frage lautet, ob die derzeit vorhandenen Mechanismen ausreichen, damit das Europäische Parlament Haushaltskontrolle ausüben kann. Dabei geht es vor allem darum, ob das EP Programme kontrollieren und/oder beeinflussen kann, die nur zum Teil aus dem EU-Haushalt finanziert werden.

Die Verfasser kommen zu dem Schluss, dass das EP zwar offiziell an der Gestaltung dieser Instrumente und an der Entscheidung, Teile des Haushalts Finanzintermediären zur Verfügung zu stellen, beteiligt ist, sodass formell Kontrolle besteht, doch ergibt sich eine Reihe von Herausforderungen aus dem Fremdvergleichscharakter dieser Kontrolle nach der Umsetzung von Kofinanzierungen. Insbesondere ist die Kontrolle eindeutig theoretisch auf einen Rahmen reduziert, in dem ein Finanzierungsinstrument über einen Intermediär (wie EIB oder EBWE) geleitet wird, der dann die Verwaltung der Auszahlung an einen weiteren Intermediär (beispielsweise eine Bank) abgibt.

- **Beziehung zwischen Kofinanzierungen und den strategischen Zielen der EU:** Eine zentrale Sorge besteht an dieser Stelle darin, dass die Arbeit mit Finanzintermediären die Prioritäten der Union verzerren könnte. Bankdarlehen benötigen immerhin Darlehensnehmer, wobei sich die Frage stellt, ob deren Interessen in Einklang mit denen der EU stehen.

Insgesamt ziehen die Verfasser hier ein gemischtes Fazit. Positiv ist zu bewerten, dass eindeutig belegt ist, dass Kofinanzierungen in Bereichen erfolgt sind, in denen erhebliche Erfolge bei der Umsetzung politischer Prioritäten der EU wie Innovation, Forschung und Wettbewerbsfähigkeit - alles grundlegende strategische Ziele der EU - erzielt worden sind. Allerdings bestehen deutliche Unterschiede bei den Möglichkeiten der „neuen“ Mitgliedstaaten und den KMU-Akteuren zur Nutzung dieser Instrumente, was Anlass zu der Befürchtung gibt, dass das Instrument der Kofinanzierung derzeit am besten für relativ entwickelte Märkte geeignet ist. Dies zeigt sich insbesondere bei den andauernden und ernstesten Problemen, die sowohl durch die Finanzkrise als auch durch den geringen Umfang der Inanspruchnahme der Strukturfonds in vielen dieser Staaten verursacht wurden - Probleme, bei denen es vielleicht unrealistisch ist anzunehmen, sie könnten durch Kofinanzierung überwunden werden.

- **Leitung und Transparenz:** Bei Kofinanzierungen wird befürchtet, dass die damit verbundenen Politikinstrumente immer komplizierter werden, was ihre politische Kontrolle, Verwaltung und Abrechenbarkeit einschränken könnte. Diese Bedenken näher zu untersuchen ist eines der Anliegen dieser Studie.

Die Verfasser kommen zu dem Schluss, dass die Transparenz durch zwei besondere Gesichtspunkte gekennzeichnet ist. Der erste Gesichtspunkt betrifft die Tatsache, dass es bei Kofinanzierungen für die EU-Organe selbst schwerer ist nachzuvollziehen, wie die Haushaltsmittel ausgegeben werden, und die Wirksamkeit dieser Ausgaben zu bewerten. Der zweite Gesichtspunkt betrifft die Spannungen, die im Falle der Kofinanzierung mit EIB und EBWE auftreten, da die EU insbesondere um Transparenz und Offenheit bemüht ist und das Streben von EIB und EBWE darin besteht, die Vertraulichkeit ihrer Geschäftsdaten zu wahren, die ein wesentlicher Teil ihrer Darlehensstätigkeit sind. Solche Spannungen sind schwer zu mindern, da sie sich zwangsläufig mit der Anwendung von Kofinanzierungen ergeben.

- **Bekanntheit:** Da an einer Kofinanzierung stets mehrere Partner beteiligt sind, die sich offenbar immer komplexerer Politikinstrumente bedienen, kann dies auch Auswirkungen für die Bekanntheit der Union bei Empfängern und Interessengruppen haben. Außerdem wird untersucht, wie die Kofinanzierung die Wahrnehmung innerhalb der EU als Ganzes beeinflusst.

Das Fazit der Verfasser lautet, dass viele EU-Programme kaum bekannt sind, das Problem bei der Kofinanzierung aber besonders akut ist. Alles in allem ergeben die Recherchen, dass die EU zwar mit einer Reihe von Programmen kontinuierlich versucht hat, ihre Bekanntheit zu steigern, Interessengruppen und Empfänger aber generell kaum etwas darüber wissen. Theoretisch ist dies kaum überraschend: Kofinanzierung läuft meist über Intermediäre, die letztlich für die Auszahlung der Gelder verantwortlich sind, sodass die Rolle der EU zunehmend aus dem Blickfeld gerät. Doch auch zwischen den EU-Organen selbst bestehen akute Probleme hinsichtlich des Bekanntheitsgrades der Kofinanzierung, da der einzigartige Charakter von EIB und EBWE kaum verstanden wird und allgemein nicht viel über die Reichweite und den Umfang von Kofinanzierungen bekannt ist.

Da in diesem Bericht zwei wichtige europäische Banken (EIB und EBWE) im Mittelpunkt stehen, sind in einer Tabelle nachfolgend diese beiden Institutionen in einem vergleichenden Überblick dargestellt.

Tabelle 1: EIB/EBWE auf einen Blick

	EIB	EBWE
Errichtet	1958	1991
Rating	AAA/Aaa	AAA/Aaa
Zielsetzung	Im Vertrag verankertes Bankinstitut der Europäischen Union für langfristige Finanzierungen. Eine Bank, die sich an politischen Vorgaben orientiert, namentlich innerhalb der EU, Kohäsion, Wettbewerbsfähigkeit, Umwelt, TEN-V, Energie und KMU sowie außerhalb der EU technische und wirtschaftliche Zusammenarbeit mit Drittländern und Entwicklung durch Finanzierung von Projekten im öffentlichen und privaten Sektor.	Förderung des wirtschaftlichen Fortschritts von MOE-Ländern durch enge und koordinierte Zusammenarbeit. Unterstützung, damit deren Volkswirtschaften international wettbewerbsfähiger werden, sowie bei Wiederaufbau und Entwicklung dieser Länder. Förderung des Übergangs zu einer Marktwirtschaft und Bereitstellung von Investitionen im privaten Sektor.
Sitz	Luxemburg	London
Anzahl der Regionalbüros	23 (11 außerhalb EU)	35
Anzahl der Mitarbeiter (Ende 2009)	1906 (EIB-Gruppe)	1492
Anteil der Mitarbeiter am Sitz	92 %	76 %
Anteilseigner	27 Mitgliedstaaten der EU	61 Länder (einschließlich aller EU-Mitgliedstaaten), EK und EIB
Größte Beteiligungen	Deutschland, Frankreich, Italien und das Ver. Königreich halten 65 % des Gesellschaftskapitals	Die EK, die EU-Mitgliedstaaten und die EIB halten mehr als 60 % des Gesellschaftskapitals
Gezeichnetes Kapital	232 Mrd. EUR	33 Mrd. EUR
Länder, in denen sie tätig sind	EU und 140 Länder weltweit	30 Länder in Mitteleuropa und Zentralasien
Gezeichnete Darlehen (2010)	72 Mrd. EUR	9 Mrd. EUR
Schwerpunkt von Investitionen	Öffentlicher und privater Sektor	Privater Sektor
Produkte	Erstrangige Darlehen, Mezzanine-Finanzierungen, indirekte Kapitalbeteiligungen, Garantien und technische Hilfe	Erstrangige Darlehen, Mezzanine-Finanzierungen, Kapitalbeteiligungen, Garantien und technische Hilfe
Durchschnittl. Darlehenshöhe	130 Mio. EUR	25 Mio. EUR
Auswahl-	-Beitrag zur Erreichung der Ziele	-Additionalität

kriterien für Projekte	der EU-Politik -Qualität der betreffenden Investitionen -Zusatznutzen durch die EIB -Subsidiarität -solide Bankpraxis	-Übergangseffekte -solide Bankpraxis
Risikokultur	Gemeinschaftsgarantie für Finanzierungen in Drittländern	Weniger als 20 % der Investitionen sind durchstaatliche Bürgschaften abgesichert
Zinsen	Zinsfestsetzung basierend auf Kostendeckung	Zinsfestsetzung basierend auf Marktbedingungen

RÉSUMÉ

Cette étude a été préparée entre les mois de décembre 2010 et de février 2011 pour la commission des budgets du Parlement européen; elle met l'accent sur les implications, pour le budget de l'Union, de l'augmentation du cofinancement, en ciblant plus particulièrement les liens avec la Banque européenne d'investissement (BEI) et la Banque européenne pour la reconstruction et le développement (BERD).

À l'occasion des délibérations relatives au cadre financier 2007-2013, les institutions de l'UE sont tombées d'accord sur la création d'instruments de cofinancement dans le but de renforcer l'effet de levier du budget de l'Union européenne afin d'augmenter la capacité de l'UE à réaliser ses objectifs stratégiques.

Pour donner suite à cette décision, le cofinancement a été augmenté: des fonds du budget de l'Union sont associés à des prêts de la BEI et de la BERD en vue d'obtenir de meilleurs résultats financiers que ceux qui pourraient être atteints autrement. Cependant, une telle activité soulève trois préoccupations précises qui sont au centre de cette étude: l'une concerne le contrôle financier et le passif financier; l'autre la gouvernance, et en particulier les questions de transparence et de visibilité; et la dernière la mesure dans laquelle cette activité favorise la réalisation des objectifs de l'Union.

Afin d'examiner ces questions, l'étude combine une analyse documentaire avec des entretiens exploratoires qui ont été menés avec plus de 50 parties prenantes essentielles et décideurs politiques de la BEI, de la BERD, de la Commission européenne et de la Cour des comptes européenne.

Les principales questions soulevées et conclusions tirées qui ressortent de l'étude sont les suivantes:

- **Engagement budgétaire:** la question de savoir si l'augmentation du cofinancement menace le budget du point de vue de l'engagement budgétaire est au centre de l'étude. Le travail avec la BEI et la BERD expose-t-il le budget de l'Union à des menaces précises en cas, par exemple, de pertes par l'une ou l'autre des banques?

En général, on constate qu'il y a en fait peu, voire pas, de préoccupations, au sens officiel, sur le plan de l'engagement budgétaire. Tous les instruments cofinancés impliquent des allocations à des programmes dont la portée est plafonnée, donc aucun de ces instruments ne pose un risque pour le budget au-delà de celui qui est pris initialement. Même dans les cas où l'instrument financier implique une forme de garantie, aucun engagement supérieur à celui initialement pris lors de la conception des instruments n'est nécessaire.

- **Le mandat extérieur:** actuellement, une grande partie des prêts extérieurs de la BEI sont réalisés sur la base d'une garantie budgétaire qui soutient les politiques extérieures de l'UE en couvrant les risques souverains et politiques. Une question centrale de cette étude consiste à déterminer si les fonds du mandat extérieur sont suffisants compte tenu des volumes de prêts actuels de la BEI, et s'ils représentent un risque pour le budget de l'Union.

Dans l'ensemble, nous sommes en accord avec les évaluations antérieures du fonds de garantie, qui ont révélé une gestion efficace, des réserves aménagées de manière adéquate et des mécanismes de gouvernance solides. Il pose peu, voire pas, de risques théoriques ou pratiques pour le budget. Nous admettons néanmoins que cela pourrait changer si la BEI venait à fortement augmenter son activité de prêt extérieur, en supposant que ce ne serait pas à ses propres risques.

- **Gestion budgétaire:** dans le rapport, chaque menace pour la discipline budgétaire est étudiée en tenant particulièrement compte a) des garanties de l'Union sur les prêts aux États membres et b) des garanties fournies à la BEI pour ses activités extérieures. Pour ce faire, nous avons dû examiner les deux méthodes de provision pour pertes suivies par l'UE. Dans le cas des garanties de l'Union sur les prêts destinés aux États membres, la provision est fournie par la marge de décaissement du budget de l'Union. Un fonds de réserve spécial (le Fonds de garantie de l'UE) prévoit des réserves pour les pertes découlant spécifiquement de la garantie de l'UE accordée à la BEI pour ses activités de prêt extérieur.

Nous concluons que les deux méthodes relatives à la provision pour pertes sont valables. Bien qu'elles soient différentes, elles fournissent toutes les deux, à leur manière respective, une protection adéquate au budget de l'Union en assurant une provision suffisante, voire peut-être excessive. Au cours des évaluations des deux méthodes (une évaluation externe du Fonds de garantie de l'UE et une évaluation interne de la marge de décaissement du budget de l'Union) des simulations des pires scénarios de non-remboursement - qui vont bien au-delà de ceux qui pourraient se concrétiser - sont effectuées, et, dans tous les scénarios testés, les mécanismes et les montants de provision ont été jugés plus qu'adéquats. Toutes les décisions liées aux prêts aux États membres et aux activités extérieures de la BEI ont été prises après que l'autorité budgétaire a été informée et a donné son accord et après que des limites strictes et concertées ont été imposées aux activités (par exemple des limites sur les volumes des prêts de la BEI).

- **Contrôle budgétaire:** une question essentielle consiste à savoir si les mécanismes en vigueur actuellement suffisent pour que le PE exerce un contrôle budgétaire. Il est également crucial de savoir si, oui ou non, le PE peut contrôler et/ou influencer les programmes qui ne sont financés qu'en partie par le budget de l'Union.

Nous concluons que malgré la participation officielle du PE à la conception de ces instruments et à la décision de mettre des parties du budget à la disposition d'intermédiaires financiers, maintenant par là des niveaux de contrôle au sens officiel, plusieurs défis sont à relever pour garantir l'indépendance de ce contrôle après la mise en œuvre du cofinancement. En particulier, le contrôle reste manifestement théorique et se limite au cadre dans lequel un instrument financier est utilisé par un intermédiaire (comme la BEI ou la BERD) qui transmet ensuite la gestion des dépenses à un autre intermédiaire (une banque par exemple).

- **Rapport entre le cofinancement et les objectifs stratégiques de l'UE:** la préoccupation principale est de déterminer si le recours à des intermédiaires financiers ne constitue pas une déviance par rapport aux priorités de l'Union. Après tout, les prêts bancaires impliquent des emprunteurs, d'où la question de savoir si leurs intérêts sont compatibles avec ceux de l'UE.

Dans l'ensemble, les conclusions sont mitigées. L'aspect positif: il est prouvé que le cofinancement a concerné des domaines qui ont connu une réussite considérable dans la réalisation des priorités stratégiques de l'UE, telles que l'innovation, la recherche et la compétitivité, qui constituent toutes les trois des objectifs stratégiques fondamentaux de l'UE. Cependant, on constate des différences considérables entre les capacités des «nouveaux» États membres et des PME à bénéficier de ces instruments, d'où les inquiétudes selon lesquelles le cofinancement pourrait être mieux adapté aux marchés qui sont relativement développés. Ce phénomène est illustré tout particulièrement par les graves problèmes causés actuellement par la crise financière et les faibles niveaux d'absorption des fonds structurels dans une grande partie de ces États; il est peut-être irréaliste d'espérer que le cofinancement résolve ces problèmes.

- **Gouvernance et transparence:** le cofinancement suscite des inquiétudes à propos des instruments politiques associés qui pourraient être de plus en plus complexes, réduisant ainsi l'attention portée aux questions du contrôle, de la gouvernance et de la responsabilité politiques. L'objet de cette étude est d'examiner ces inquiétudes.

Nous concluons que la question de la transparence revêt deux aspects particuliers. Premièrement, le cofinancement ne fait que compliquer la tâche des institutions de l'UE elles-mêmes, consistant à surveiller la façon dont le budget est dépensé et à évaluer l'efficacité de ces dépenses. Deuxièmement, il y a des tensions au cœur du cofinancement avec la BEI et la BERD, en particulier en ce qui concerne l'aspiration de l'Union à la transparence et à l'ouverture et celle de la BEI et de la BERD au respect de leur confidentialité commerciale, qui est essentielle à leurs activités de prêt. Il est très difficile de réduire ces tensions car elles sont au cœur de l'adoption du cofinancement.

- **Visibilité:** étant donné que le cofinancement implique des partenaires multiples, pour des instruments politiques qui semblent de plus en plus complexes, il pourrait y avoir des implications également pour la visibilité de l'Union au niveau des bénéficiaires et des parties prenantes. Nous examinons également les répercussions du cofinancement sur la visibilité de l'Union dans son ensemble.

Nous concluons que dans un contexte où la visibilité de nombreux programmes européens est mauvaise, le cofinancement pose des problèmes particulièrement graves en la matière. Dans l'ensemble, bien que l'UE essaie systématiquement de développer plusieurs programmes visant à améliorer la visibilité, nos conclusions indiquent une mauvaise connaissance des parties prenantes et des bénéficiaires à tous les niveaux. Sur le plan théorique, ce n'est pas une surprise, le cofinancement a fréquemment recours à des intermédiaires, auxquels il revient en fin de compte d'exécuter les fonds, ce qui rend le rôle de l'Union de plus en plus opaque. Cependant, des problèmes graves de visibilité se présentent aussi entre les institutions de l'UE elles-mêmes, qui ont une mauvaise compréhension des natures particulières de la BEI et de la BERD et une mauvaise connaissance de la portée et de l'échelle du cofinancement.

Comme ce rapport se concentre sur deux banques européennes clés (la BEI et la BERD), voici un tableau récapitulatif qui compare «d'un coup d'œil» ces deux institutions.

Tableau 1: BEI/BERD en un coup d'œil

	BEI	BERD
Fondation	1958	1991
Notation	AAA/Aaa	AAA/Aaa
Objectif	L'institution de prêt à long terme de l'Union européenne créée par le traité. Une banque axée sur la politique soutenant les objectifs prioritaires de l'UE; à l'intérieur de l'UE: la cohésion, la compétitivité, l'environnement, les RTE, l'énergie et les PME; à l'extérieur de l'UE: la coopération technique et économique avec des pays tiers, et le développement au moyen d'opérations de financement dans les secteurs publics et privés.	Promouvoir la progression économique des PECO grâce à une coopération étroite et coordonnée. Aider leurs économies à devenir plus compétitives sur le plan international et les assister dans leur reconstruction et leur développement. Favoriser la transition vers l'économie de marché et fournir des investissements privés.
Siège	Luxembourg	Londres
Nombre de bureaux régionaux	23 (11 à l'extérieur de l'UE)	35
Nombre d'employés (fin 2009)	1906 (groupe BEI)	1492
% employés au siège	92 %	76 %
Actionnaires	27 États membres de l'UE	61 pays (dont tous les États membres de l'UE), la CE et la BEI
Principales participations	La France, l'Allemagne, l'Italie et le Royaume-Uni détiennent 65 % du capital social	La CE, les États membres de la CE et la BEI détiennent plus de 60 % du capital social
Capital versé	232 milliard d'EUR	33 milliards d'EUR
Pays d'opérations	UE + 140 pays dans le monde	30 pays d'Europe centrale et d'Asie centrale
Vol. des signatures de prêts (2010)	72 milliards d'EUR	9 milliards d'EUR
Cible des investissements	Secteurs publics et privés	Secteur privé
Produits	Prêts privilégiés, financement secondaire, participations indirectes, garanties et assistance technique	Prêts privilégiés, financement secondaire, actions, garanties et assistance technique
Taille moyenne des prêts	130 millions d'EUR	25 millions d'EUR
Raisons de sélection des projets	-Contribution aux objectifs stratégiques de l'UE -Qualité des investissements sous-jacents -Valeur ajoutée par la BEI -Subsidiarité -Gestion bancaire saine	-Additionnalité -Impact sur la transition -Gestion bancaire saine
Culture du	Garantie communautaire pour	Moins de 20 % des

risque	les prêts extérieurs	investissements ont une garantie souveraine
Fixation des prix	Fixation des prix basée sur le recouvrement des coûts	Prix fixés sur le marché

1. INTRODUCTION

This study has been prepared by Dr. Nick Robinson (University of Leeds) and Dr. Robert Bain (an independent consultant) in response to the specific contract IP/D/BUDG/IC/2010-153 for a study on 'The implications of EIB and EBRD co-financing for the EU budget'.

The introduction offers a brief assessment of the objectives of the study (section 1.1), the methodology used (section 1.2) and provides an overview of the report's structure (section 1.3).

1.1. Objectives

This report identifies the following key areas for investigation, which are derived from the terms of reference as set by the EP's committee on budgets, and can be summarised as follows:

- an **inventory and evaluation of the strategic approach** within the EU budget in light of the growth of off-budget funding through EIB and EBRD loans. The study sets out the growth, scope and detail of the operations undertaken by the EIB and EBRD which also receive funds from the EU budget. The study places such activity within a more broad ranging strategic overview of the EU's activity, as a whole, and of the growth of the EIB and EBRD's specific activity.
- an overview of the key issues centred on **budgetary management**. In particular, the report offers an evaluation of the key threats to budgetary discipline which are offered by the possibility of loan default in a climate of increasing fiscal stress and of increasing co-financing. The latter has potential implications for the budgetary discipline of the EU as a whole and is explored here. Questions of budgetary management also raise issues in relation to loan default. The report also compares two different approaches to funding default and loan guarantee which are offered by the loan guarantee fund (which provides a guarantee within the EU budget against loan default) and the guarantees to loans offered to the member states which are not funded from the EU budget.
- an evaluation of the issues centred on the **external mandate**. There have been a number of recent EU policy innovations in the area of activity undertaken outside the Union, most particularly seen in the form of the external mandate, which refers to the budgetary guarantee which underpins EU external policies covering sovereign and political risks. Of central concern to this study is the following: an evaluation of the synergies and practical problems associated with the blending of EU grants and EIB loans; the issue of EU budget guarantees for sovereign debt, and the synergies and problems which are presented in combining EU grants, EIB and EBRD loans, with particular focus on the balance which should be struck between financial and political considerations.
- discussion and evaluation of the key issues in relation to **governance and accountability**. Co-financing raises potentially important issues in terms of governance and accountability, prompted by the fact that while the Commission is accountable to the European Parliament for policies which are funded by the EU

budget, the EIB is owned by the member states and hence accountable to them through its board of governors. Furthermore, the increasing complexity of the policy mechanisms which are created through the growth of EIB/EBRD and EU budgetary collaboration in the form of co-financing arrangements and loan-grant blending also raise implications for governance and accountability given the different accountability mechanisms in place.

- an evaluation of the mechanisms which the EP has to maintain **budgetary control**. The key issue is the extent to which the creation of innovative financial instruments makes the EP's job more difficult in terms of exercising budgetary control. While the EP is formally involved in the framing of these instruments, and in the decision to place parts of the budget at the disposal of financial intermediaries, so arguably maintaining formal levels of control, a number of challenges present themselves in terms of the arms-length nature of that control and the extent to which implementation becomes progressively detached from the operational influence of the Parliament and Commission. The key question is how the EP can control and/or influence programmes which are only part funded by the EU budget.
- finally, the study examines questions of **transparency and visibility**, with particular focus on exploring how the visibility of the EU's budgetary contribution can be guaranteed in areas in which there is part financing by the EIB/EBRD. In the case of transparency, tensions potentially exist between the EP's desire for openness alongside the EIB and EBRD's desire to respect their commercial confidentiality, which are central to their lending activity. Visibility relates to the extent to which stakeholder knowledge of EU policies is affected by co-financing, addressing whether the growth of policy intermediaries serves to help or hinder visibility.

The cumulative implications of the consideration of these individual objectives allows for the study to offer some comments which can contribute to a macro level evaluation of the EU's strategic approach in light of the EU2020 agenda and the growth of EIB and EBRD activity.

1.2. Methodology

The study adopts a combination of desk-based documentary analysis with exploratory interviews with key stakeholders and policy makers from the EIB, EBRD, European Commission and European Court of Auditors.

The methodology was validated in a scoping and validation meeting held in the European Parliament on 30th November 2010.

1.2.1. Desk Research

Desk-based documentary analysis has been conducted with the aim of reviewing the specific material on EU-EIB and EU-EBRD co-financing. Documents produced by the EP, EIB, EBRD and European Commission were read in order to establish the scope of EU co-financing and to ascertain the present status of evaluation. These documents were used to compile the inventory (Annex 1) and to inform the analysis (Chapters 3 and 4).

Documentary analysis was also undertaken to inform the contextual discussion, so placing the growth of EU co-financing in terms of the growth of EIB and EBRD lending activity more generally (Chapter 2).

The authors wish to thank officials from the EIB, EBRD, EP and European Commission for their help with sharing documentary sources and information. A list of those who have spoken to us as part of this study is given in the appendices.

A list of the principal documentation used is given in the references at the end of this report.

1.2.2. Interviews and Fieldwork

The interviews were undertaken on three fieldwork trips: to Brussels, centred on interviews with EU officials and policy makers; to Luxembourg, centred on interviews with EIB officials and members of the European Court of Auditors, and to London, centred on interviews with EBRD officials. The interviewees were selected due to their specific expertise in the area of EU-EIB/EBRD co-financing and encompassed those with an expertise of both the EU's internal and external activity.

These interviews were specifically designed to gain answers to the questions set out in the objectives above with respondents being probed as to the implications for finance, governance, policy, liability, budgetary management and visibility as appropriate. In particular, questions were asked in terms of:

- issues related to the growth of co-financing over time, the implications of the financial and economic crisis and the prospects for future growth;
- issues related to the alignment between EU and EIB/EBRD policy objectives;
- issues related to the EIB/EBRD's initiatives which are guaranteed by the EU and the financial vulnerability of such instruments;
- issues related to governance, control, transparency and visibility and the extent to which they are affected by the growth of co-financing;
- specific issues related to the external mandate in particular centred on the synergies between EU grants and EIB/EBRD loans and in terms of the practical implications of collaboration;
- finally, issues related to the likely future development of EU-EIB/EBRD collaboration and the future proposals in this area.

The authors wish to thank officials from the European Court of Auditors, EIB, EBRD and European Commission for their time and assistance with the interview process.

A list of the interviewees is given in Annex 2 at the end of this report.

1.3. Report Structure

The remainder of the report is based on the following sections.

- As our study focuses on the EU's role specifically in relation to the two banks (the EIB and the EBRD), these banks are introduced in Chapter 2. The review of the banks builds on published documentation and from the findings from our interviews. When discussing our terms of reference with various parties, it became obvious that there were some misconceptions about the banks, their roles, capabilities and capacities. We sought to address these misconceptions by providing detail in our report about the banks themselves, before extending our discussion to consider the co-financing arrangements with them.
- Chapter 3 provides an evaluation of the development of co-financing instruments within the European Union, explicitly addressing the questions raised within the terms of reference of this study in relation to co-financing between the EIB and EBRD. The analysis, which draws extensively on the empirical findings which were derived from the fieldwork interviews, covers the following: whether co-financing poses any budgetary risks, covering both strictly financial elements and questions of control more broadly; the relationship between co-financing and the delivery of the strategic objectives of the EU; transparency, particularly in terms of affects on the EU institutions; issues related to visibility, with particular focus on the beneficiaries, and whether there is a trade off between political and financial considerations in this area.
- Chapter 4 examines guarantees extended by the EU that could make a call on the EU budget. The first section considers guarantees for 'indirect lending' (guarantees to the EIB for EIB lending to third countries). The second section looks at EU budget guarantees for 'direct lending' (loans extended to Member States). Each separate form of guarantee instrument is described – including its application and method of operation – before the implications for the EU budget are explained.
- Chapter 5 offers the study's overall conclusions and recommendations.
- Chapter 6 considers issues raised during our research which, although related to our study, were not identified as key questions to be addressed in our Terms of Reference. The topics, which include the future of co-financing, questions of standardisation in relation to co-financed instruments and 'using the EIB and EBRD to maximum effect', were identified from our reviews of EU and bank reports and from our interviews with Commission, Bank and Court of Auditor's staff.
- Finally, of particular importance to this study is the recent growth of EIB/EBRD co-financing and blended instruments – Annex 1 offers a detailed inventory of such activity, setting out its scope and scale.

2. THE BANKS: OVERVIEW

By way of introduction this chapter compares and contrasts the two banks under consideration: the EIB and the EBRD. Summary highlights – of particular relevance to this study – are presented in relation to:

- Institutional objectives;
- Ownership and voting rights;
- Management structure;
- Balance sheet analysis;
- Lending volumes;
- Financial risk management;
- Key credit features.

2.1. Institutional objectives

2.1.1. The European Investment Bank (EIB)

The EIB was established in 1958 under the Treaty of Rome to act as the long-term financing institution of (what is now) the European Union, with a specific mission to support EU policy objectives by financing investment. This is a different and broader mandate than most International Financing Institutions (IFIS). For lending within the EU (and to pre-accession and candidate countries) the Bank's objectives include providing support for economic and social cohesion and convergence, economic innovation, intra-EU transportation, SMEs, environmental protection and sustainability, and competitive and secure energy. Importantly, since 2010, climate action has been a priority objective for EU lending operations.

Outside the EU, objectives include support for pre-accession initiatives, private sector development, financial sector development, infrastructure, securing energy supplies, environmental protection and improvements – and EU 'presence' (foreign direct investment, transfer of technology and know-how).

Since the onset of the current global financial crisis, the Bank's shareholders requested it to ramp-up its operations in response to financial stress in member countries – which it has done (see later on lending volumes).

2.1.2. The European Bank for Reconstruction and Development (EBRD)

The EBRD was established in 1991 for a specific purpose: to foster the transition towards open-market orientated economies in Central and Eastern Europe, and the Commonwealth of Independent States (CIS – former Soviet countries). It pursues its objective by promoting

private and entrepreneurial initiatives in the countries it has committed to by applying the principles of multi-party democracy, pluralism and market economics.

The Agreement establishing the Bank requires an annual review to be undertaken of its strategy in each country of operations, encompassing the respective country's progress on decentralisation, de-monopolisation and privatisation. In cases where a member implements policies inconsistent with these objectives, the Board of Directors can recommend to the Board of Governors that access to EBRD resources be limited or suspended.

2.2. Ownership and Voting Rights

2.2.1. The EIB

EIB's membership comprises the 27 EU Member States (EU-27). The most recent countries to join were Romania and Bulgaria (January 2007). The largest shareholders are Germany, France, Italy and the UK (each with 16.17% of share capital).

The Statute of the European Investment Bank incorporates specific legislation governing the Bank. As a protocol annexed to both the Treaty on European Union and the Treaty on the Functioning of the European Union, the Statute has the same legal force (i.e. primacy over the national laws of EU Member States which can be enforced through the EU Court of Justice).

Some of the decisions of the EIB's Board of Governors must be unanimous (such as those to increase subscribed capital and the determination of the proportion that has to be 'paid in'). Other decisions of the Board must be supported by a vote of a majority of Members accounting for at least 50% of subscribed capital. Decisions of the Board of Directors, including to call callable capital, must be taken by a vote of at least one-third of Members, accounting for at least 50% of subscribed capital. In those cases where a qualified majority is called for, that majority must consist of 18 voting members (accounting for 68% of subscribed capital).

2.2.2. The EBRD

Membership of the EBRD is restricted to European countries, non-European countries (that are IMF members) and the EU and EIB. A majority of the capital stock must be held by EC member countries, the EU and the EIB (EU member countries, the EU and the EIB currently hold 63%).

The EBRD has 61 member countries: the EU-27 (ten of which are countries of operations), 20 other countries of operations including Turkey (which joined in 2008), four other European countries including Switzerland, and ten non-European countries including the USA and Japan.

Of its 30 countries of operations, the Czech Republic has been the first (and only one) to 'graduate' from new operations (in 2007). This acknowledged the country's transition to a full market economy and democracy. The global financial crisis has delayed the graduation of the remaining EU-8 countries. However Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia and Slovenia could graduate over the next five years. The USA is the EBRD's

largest shareholder (with around 10% of voting rights), followed jointly by Japan, the UK, France, Germany and Italy.

2.3. Management Structure

2.3.1. The EIB

The EIB's senior governing body is its Board of Governors comprising of one government minister (usually the minister of finance) from each Member State. It defines the general policies of the Bank and ensures their implementation.

A Board of Directors is comprised of 28 directors and 18 'alternative directors'. One is nominated by each Member State and one by the European Commission. Directors are appointed for five-year terms. Unusually, the Board 'co-opts' six non-voting experts; three as members and three as alternates.

The Bank's management committee consists of a president (currently Philippe Maystadt, ex-deputy prime minister and finance minister of Belgium) and eight vice-presidents; appointed for six-year terms. The management committee is responsible for day-to-day operations. Decisions to grant loans or extend guarantees are, however, subject to Director approval.

The Bank's staff totalled around 1,700 (in 2009). Despite this, its assets and loans-per-employee are well above those of other IFIs. The Bank is headquartered in Luxembourg and has 11 offices in other EU countries.

2.3.2. The EBRD

All powers of the EBRD are vested in its Board of Governors (one appointed by each shareholder). The Board of Governors retains the more important powers – admitting (and suspending) members, increasing the capital base and electing the president – while others are delegated to the Board of Directors.

The Board of Directors consists of 23 members. Directors are appointed for three-year terms. At the end of 2009, the EU, the EIB and the six largest shareholder countries each had their own director. The other 15 directors represent multi-country constituencies.

The Board of Governors elects the Bank's president for a four-year term. The current president is Thomas Mirow (ex-State Secretary in Germany's Federal Finance Ministry). The president may be removed by a two-thirds majority vote of governors (representing two-thirds of voting rights).

At the end of 2009, the Bank employed around 1,500 staff, most of whom (three-quarters) were based in its London headquarters. The remainder of staff work in 35 regional offices in 27 of the Bank's countries of operations.

2.4. Balance Sheet Analysis

2.4.1. The EIB

The EIB is the world's largest multilateral development bank as witnessed by its balance sheet which, at the end of 2009, showed total assets (principally loans, but also reserves, investment securities and physical assets) of EUR 362 billion. To put this in context, that is 85% more than the World Bank (assets totalling EUR 197 billion). A very large percentage of the EIB's assets (87%) are loans. A consequence of this is that the EIB's liquid assets, as a percentage of total assets, are lower than those for most other IFIs. Any liquidity concerns, however, are more than offset by, for example, the Bank's superior access to capital markets and its very strong claim to expect support from its highly-rated shareholders (which could, in principle, be enforced through the EU Court of Justice).

2.4.2. The EBRD

The EBRD's balance sheet records total assets of EUR 33 billion (end 2009), around 9% of the respective EIB figure. Other noteworthy features include the presence of substantial equity investments among the Bank's assets – which differentiates it from most other IFIs. The balance sheet also shows a still comparatively high level of shareholder equity relative to loans and investments.

The global financial crisis made a significant impact on the EBRD's balance sheet; the fall in equity valuations leading to a notable fall in the Bank's equity portfolio. The Bank recorded a net loss in 2009 – mainly due to increased provisioning against potential future loan losses. This loss (EUR 746 million) followed another loss (EUR 602 million) recorded in 2008; the first year that the Bank had not posted a profit in a decade. Despite this, the EBRD remains a stable, very well-capitalised banking operation.

2.5. Lending Volumes

The EIB's annual lending volumes since the Bank was established are presented in Figure 1. In 2010, the Bank lent EUR 71.8 billion. The EBRD's lending volumes since inception are shown in Figure 2 – but note the use of different horizontal and vertical axis scales between the two figures. In 2010 the EBRD lent EUR 9.0 billion.

Figure 1: EIB Lending Volumes since Inception

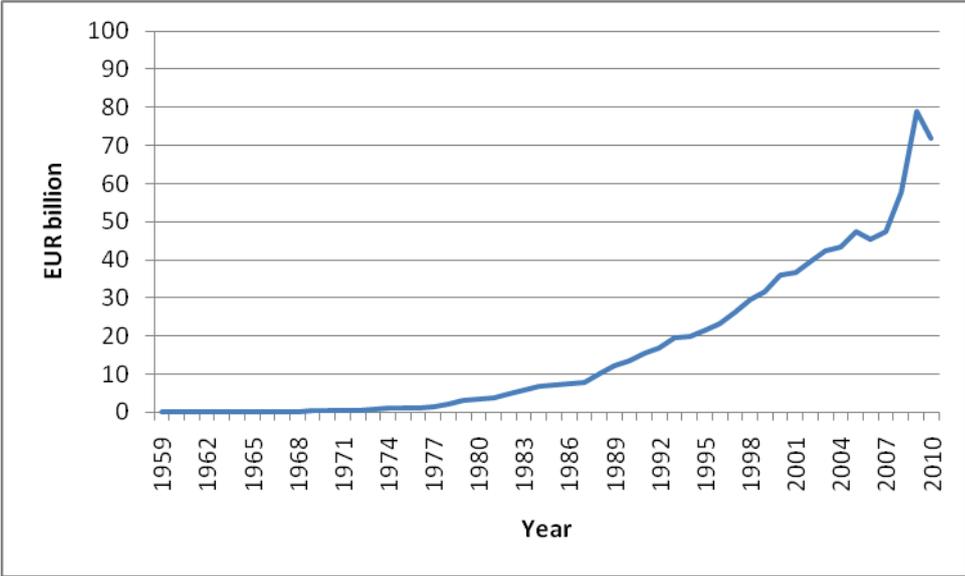
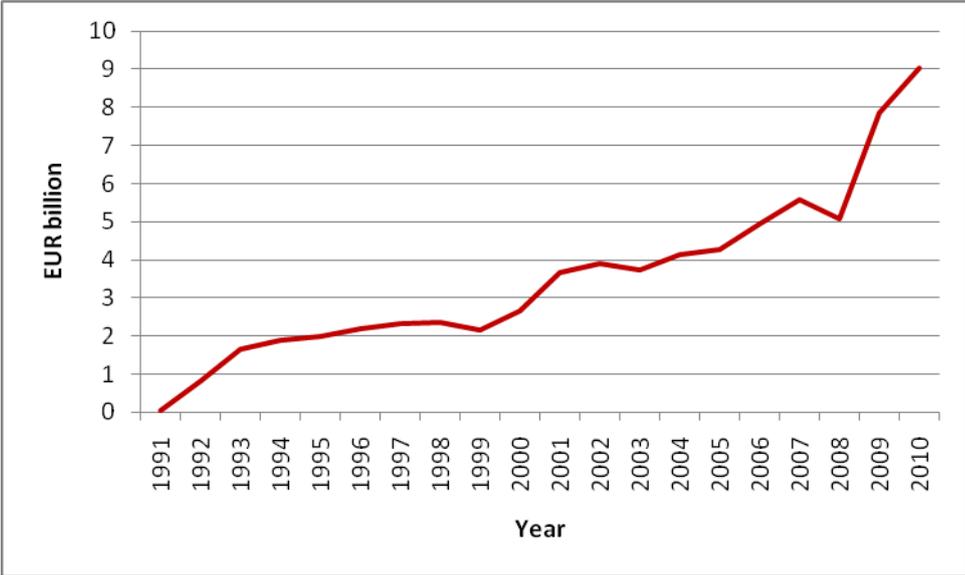
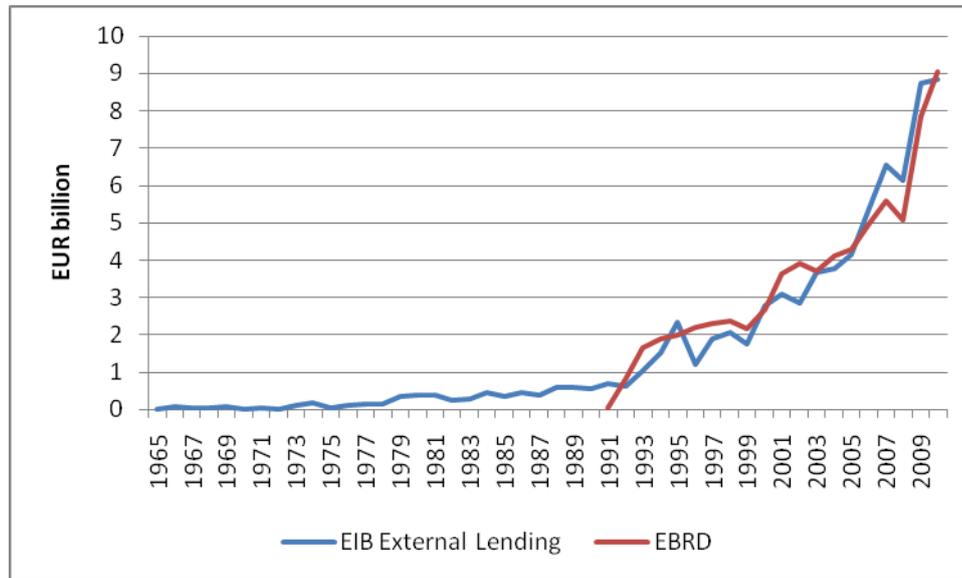


Figure 2: EBRD Lending Volumes since Inception



A comparison of total lending volumes for each bank is not truly a like-for-like comparison. In the context of this study, it is more insightful to compare the EIB's external lending activity (volumes) with those of the EBRD. That comparison is shown in Figure 3. As can be seen, the volume of activity (profile of annual disbursements) is nearly identical for each of the two banks.

Figure 3: Comparison of EIB External Lending and EBRD Lending Volumes

2.6. Financial Risk Management

2.6.1. The EIB and the EBRD

Both the EIB and EBRD have a relatively conservative attitude to treasury and asset liability management (ALM) risks. The banks hold highly rated securities and generally deal with highly rated counterparties. Although the EBRD seeks to earn more from its treasury activities than most other IFIs, systems are in place to measure and monitor risk, and contain it within acceptable limits.

EBRD's treasury portfolio was impacted by the downfall of Lehman Brothers which triggered a provisioning charge of EUR 127 million in 2008. A further charge of EUR 32 million was made in 2009 to cover securities wrapped by monolines – which the bank now assesses on a stand-alone basis.¹ The rating agencies comment that future treasury losses are expected to remain very small.

Both banks enjoy the liquidity benefits of strong access to capital markets. This offsets the fact that the EIB maintains lower levels of liquidity than some other IFIs. In terms of liquid assets as a percentage of gross debt, the figure for the EIB is 13% whereas the EBRD has 62% (the World Bank has 29% and the IADB has 34%). The liquidity position at the EIB also benefits from a very strong (legal) claim on shareholder support. The liquidity position at the EBRD is reported to be such that the bank could continue to operate normally for three years without having recourse to the capital markets.

¹ A 'monoline' (short for monoline insurer) is an insurance company with just one – hence 'mono' – specialised line of business. Multiline insurers, on the other hand, are engaged in multiple lines of business – such as coverage for property and casualty risks. Monolines provide bond insurance services. The insurance company guarantees the full and timely repayment of bond principal and interest in the event of a debt issuer default.

In terms of sectors financed, the largest exposure of the EIB is to transportation, then energy and other forms of infrastructure. The EBRD has traditionally had a large exposure to the finance sector at around 50% of total investment (although this was probably overstated as many loans to the financial sector are subsequently on-lent for specific purposes/projects).

In terms of countries of operations, at the end of 2009 93% of the EIB's loans were for projects within the EU. The overall quality of its loan portfolio is, therefore, very high – unlike most other IFIs. The EIB's five countries of largest exposure were Spain ('AA'), Germany ('AAA'), Italy ('A+'), France ('AAA') and the UK ('AAA'). In addition, as explained later, much of the EIB's activity outside of the EU benefits from an EU guarantee. The EBRD's countries of largest exposure are Russia ('BBB'), the Ukraine ('B+') and Romania ('BB+'). However the Bank limits its exposure in any individual country to 90% of paid-in capital.²

Further detail on the country-related credit quality of bank lending is measure by the rating agencies through an index (an exposure-weighted average of the default rates associated with long-term sovereign ratings). The lower the index, the lower the risk exposure. Given comments made above, it is perhaps unsurprising that this index is 1.3 for the EIB (and even that might be overstated). The same index for the EBRD is much more typical of IFIs at 6.1. For comparison purposes, the index for the World Bank is 5.1 and for the IADB is 7.1.

Capital adequacy is an important concept in banking. It measures the extent of loss that an entity can sustain before its liabilities exceed its assets. In other words, the sufficiency of funds available to meet business and regulatory objectives. Various metrics can be used, the most common of which focus on 'risk bearing capacity'. Narrow risk bearing capacity (NRBC) is equal to the sum of allowances for losses on loans (and, if applicable, losses on equity investments and guarantees) and shareholders' equity. Effectively this is the loss 'cushion'; the capacity to absorb losses. Broad risk bearing capacity (BRBC) adds callable capital from 'AAA' countries to NRBC (which, particularly in the case of the EIB, is significant).

This is not the place for an extended discussion on the mechanics of NRBC and BRBC calculations in the context of the EIB and the EBRD. The rating agencies report in some detail on such matters. Suffice to say that, in the rating agency surveillance reports, the risk bearing capacity of the EIB is described as 'far above [that] of the highest-rated commercial banks and largely reflects the high quality of the bank's assets'. Referring to the EBRD, the agencies conclude that the bank 'enjoys an extremely strong capital position...in absolute terms and relative to other "AAA" rated IFIs'.

Recently, both banks have significantly increased their lending operations in direct response to the global financial crisis. This demonstrates bank capabilities and capacities (outside of normal operations) that are seldom acknowledged from a public policy perspective. If required, additional lending can be ramped-up by both the EIB and EBRD, in significant volumes, relatively quickly. At the EIB, from 2008 to 2009, loan signatures increased by 37%. The EBRD increased its investments by more than 50% in 2009. A return to pre-downturn lending levels is anticipated beyond 2011/12.

In closing, on financial risk, it should be emphasised that both the EIB and the EBRD – like other IFIs – enjoy 'preferred creditor status'. This further reduces risk to the banks. It means that, during any period of political or economic turmoil in a particular country – when restrictions and controls on foreign currency payments can be imposed – governments would

² For an explanation of the rating scale please refer to Annex 2.

not likely prevent payment to an IFI. Instead, the host government would most likely place priority on EIB or EBRD loans specifically to maintain access to financial support.

2.7. Key Credit Features

2.7.1. The EIB and the EBRD

Research published by the rating agencies (Standard & Poor's and Moody's) summarises the key factors that underpin the credit ratings for the EIB and the EBRD (see Table 2). Many of these points have been noted and commented upon in earlier sections of this report.

Table 2: Major Credit Rating Factors

EIB	EBRD
<i>Strengths</i>	
Strong asset quality compared with other IFIs.	Extremely strong capital position, enhanced by almost EUR 9 billion in callable capital from 'AAA' rated members, and ample liquidity.
Expected continuing support from committed and highly-rated shareholders.	Prudent financial management and policies.
Relatively high capital adequacy ratio.	Excellent franchise value, reflecting EBRD's status as the largest multilateral provider of finance to its countries of operations
<i>Weaknesses</i>	
High individual country loan exposure.	A riskier portfolio of development-related exposure than most other multilaterals, due to a predominant private sector focus and large equity exposure.
High leverage relative to shareholder's equity.	

Source: Standard & Poor's (2010)

The comments summarised in Table 2 – with strengths far outweighing any weaknesses – have to be placed in context. Both agencies rate the EIB and the EBRD similarly ('AAA'/Stable); the highest possible credit standing. This is reflected in positive comments made and conclusions drawn about the EIB and EBRD in Standard & Poor's most recent research publications (October and December 2010) respectively. In the absence of government support, only one commercial bank in the world has a 'AAA' rating; Rabobank in the Netherlands.

3. CO-FINANCING IN THE EU

3.1. Introduction

This chapter provides an evaluation of the development of co-financing instruments within the European Union. After a brief discussion of the motives for co-financing, the first section sets out the debates on the strengths and weaknesses of co-financing in comparison to pure grants or loans. The second section reviews the existing evaluations which have been undertaken of the principal new financial instruments, showing the strengths and weaknesses of the present analysis. Finally, section three explicitly addresses the questions raised within the terms of reference of this study in relation to co-financing with the EIB and EBRD. This section analyses the following: whether co-financing poses any budgetary risks, covering both strictly financial elements and questions of control more broadly; the relationship between co-financing and the delivery of the strategic objectives of the EU; transparency, particularly in terms of effects on the EU institutions; issues related to visibility, with particular focus on the beneficiaries, and whether there is a trade off between political and financial considerations in this area.

3.2. Why co-financing?

As part of the deliberations over the Financial Framework 2007-13, the EU institutions reached agreement on the development of co-financing instruments with the aim to 'reinforce the leverage effect of the European Union budget' (CEC, 2010a, p. 3) in order to increase the EU's capacity to deliver on its strategic objectives. A number of the interviewees emphasised that whilst co-financing is presently very small (accounting for little more than 1% of the EU's budget) that all of the indications are that it is set to grow, given the expectation that the budget will remain 'very flat'.

The attractiveness of co-financing instruments has become even greater in light of the financial and economic crisis which has led to considerable structural difficulties with accessing funds on the financial markets (CEC, 2009, p. 4; p. 5), raising pressing needs to increase access to loan finance, for example, in the SME and research and innovation sectors (GHK, 2010b; Mann et al, 2010).

The intention of co-financing is to develop a variety of instruments such as guarantee schemes, risk-sharing facilities, technical assistance and interest rate subsidies with the aim of acting as a catalyst for private and public investors (CEC, 2010a, p.3). These instruments 'engage EU budget resources through a delivery chain of financial intermediaries starting from the EIB Group, through to the banking system, national guarantee institutions, venture capital investors and the capital markets all the way down to public or private financial beneficiaries. These financial intermediaries act as multipliers by attracting outside finance to support investments targeting EU policy priorities and addressing specific market failures' (CEC, 2010a, p.3). At a cumulative level, co-financing should help to 'align the operational priorities of all financial intermediaries in the delivery chain with the policy priorities of the European Union, while, at the same time, increasing the visibility of EU action' (CEC, 2010a, p.3).

3.2.1. Costs and Benefits of Co-Financing

The Commission report (CEC, 2009a) of the 'Working Group on the additionality of grants in the framework of blending mechanisms' provides a particularly useful overview of the scope of the benefits and costs of co-financing instruments. While this report is specifically centred on the implications in terms of the external activity of the EU, the themes raised are clearly of importance to all of the EU's activity with such instruments, whether conducted internally or externally.

The report emphasises that in general, loan grant blending (LGB) instruments serve to lower the rate at which a project becomes financially viable and reduce the risks associated with a project to the investor/financier. In terms of providing a justification for the use of such instruments, the report points out that intervention is justified in cases of market failure; when LGB instruments would serve to enhance the level of development in under-developed economies, or when the costs and benefits to external actors are greater than those for local stakeholders such that the positive externalities which would accrue from the project justify external LGB instruments as a corrective to a situation which would otherwise not deliver the benefits desired (CEC, 2009, p.6).

The report highlights the following particular benefits for financial institutions and investors which it subdivides under the following headings:

- *strategic and policy benefits* (for example, enabling the EU to deliver on those policy priorities which are not fundable through pure market instruments or ensuring the effective supply of public goods such as those projects which whilst delivering 'a positive overall social return' are not financially sustainable due to insufficient financial return (CEC, 2009, p.7));
- *financial benefits* (for example enhancing financial leverage so gaining greater support for EU priority projects and/or support for those schemes which are deemed to have desirable impacts such as in the area of environmental sustainability; lowering risk, so making projects more feasible; or increasing flexibility by varying the relative contribution of the grant/loan on the basis of the particular needs of the project to enhance deliverability);
- *operational benefits* (such as greater financial discipline across the project life-cycle; enhanced expertise, particularly in terms of the project management skills of the loan provider; the acceleration of the initial phases of the project, particularly through technical assistance in the areas of project preparation and capacity building; enhancing the strength of the co-ordination between the project donors; and knowledge transfer and policy learning in which the project lender is able to use their experience to demonstrate examples of best practice to enhance the return on the investments (CEC, 2009, p.7-8).

The report also identifies the following potential weaknesses of a focus on loan-grant blending (CEC, 2009, p.9-10):

- *economic risks* (in particular, crowding out which occurs in cases in which other sources of finance are available such that the project remains viable without loan-grant blending. In such circumstances loan-grant blending should be avoided as it would serve to undermine the capacity of the financial markets; also market

distortion exists as a very real possibility if the beneficiary gains an unfair advantage over its local or international competitors);

- *financial risks* (in complex projects of interest to multiple donors there may be a risk that the donors are played off against each other resulting in excessive donor support; a desire to secure prestige project may lead to imprudent practice facilitated by pressure from stakeholders and donor support which results in projects being financed which have limited economic viability; risks may be simply transferred to the donor (e.g. the EU) rather than mitigated because the existence of loan-grant blending may reduce the incentives for the project instigator to assess risk)
- *operational risks* (e.g. a lack of visibility and transparency which may occur either through a decline in control over funds or a lack of visibility in comparison to projects with a direct project contribution; slow-down of decision making can occur due to difficulties of co-ordination of multiple project partners. For example, diverging rules, procedures and priorities may slow the project process and increase costs, particularly in the initial phases).

A recent report of the Overseas Development Institute (ODI, 2011), *EU Blending Facilities: Implications for Future Governance Options*, built upon the Commission and EIB's earlier published work to provide an in-depth investigation of the costs and benefits of the usage of blended mechanisms in contrast to either pure grants or loans, coming to very similar conclusions (ODI, 2011, p.15-19). This report was also based on an evaluation of such mechanisms within regions outside the EU but its findings have clear applicability for this study, with the following insights being of particular importance (ODI, 2011, p.19):

Compared to pure loans, blending mechanisms:

- do not serve to significantly exacerbate levels of indebtedness because of the presence of the grant component serves to reduce the scale of the loan required for the project's realisation;
- allow positive externalities by helping to facilitate projects with high environmental or social benefit which would otherwise struggle to attract investment on a strictly commercial basis;
- enhance the quality of projects either through the existence of technical assistance or through the commitment of the co-financier to the project's quality;
- enhance ownership of the project as the recipient country has greater control and stake than in a pure loan situation;
- enhance EU visibility and strengthen donor co-ordination.

However, the report also offered a number of warnings if the benefits of loan-grant blending are to be realised. In particular, there needs to be:

- a reduction in complexity with frameworks which are simplified in order to enhance accountability and responsibility to ensure transparency;
- a conscious effort to avoid crowding out of other potential sources of funding;

- a focus on preventing excessive borrowing, particularly if the existence of loan-grant blending opportunities encourages borrowing which is unprudential;
- a focus on avoiding the slowing of decision making due to complexity and the existence of multiple stakeholder interests;
- the capacity for donor countries to maintain their visibility so ensuring they have the incentives to participate in loan-grant blending;
- a focus on ensuring that the policy objectives remain central to the principles which drive the disbursement of public funds rather than the financial imperatives of the lender.

As part of the fieldwork for this report, interviewees were extensively probed on the strengths and weaknesses which could be derived from using co-financing. Perhaps unsurprisingly, given the nature of the interviewees, they saw such instruments as highly beneficial: working with the private sector was in and of itself of benefit, with private expertise offered in terms of technical assistance. Co-financing was seen as crucial in addressing resource gaps in both national budgets and IFI and bank lending capacity; as a method of connecting the individual ‘who was lost in Brussels’ much closer to the EU; as a way of delivering projects which would offer genuine EU ‘added value’; as a means of reducing waste, which was acknowledged as a historical problem with multiple ‘consultancy studies which have produced no investments’; as a way of increasing incentives, and as a means of helping with institutional capacity building and the modernisation of developing economies, with the ultimate aim of developing markets. To this degree, interviewees raised many plus points for such instruments, many of which will be discussed within this chapter.

3.3. Evaluations of existing mechanisms³

Given the newness of many of these instruments, evaluations of their effectiveness are understandably relatively limited. However, a number of studies have been conducted by a combination of the European Commission, European Investment Bank and consultants operating on behalf of the EU.

At present, only two innovative financial instruments have been evaluated by a combination of EU commissioned experts and EU institutions: the RSFF (two evaluations, one by the EIB and one by an EU commissioned expert group) and the CIP (two evaluations - one by the Commission in the form of its annual implementation report and one by an expert group which has produced a series of reports).

Thus the remaining financial instruments which have been evaluated at all have only been evaluated by EU institutions - in some cases this has come in the form of evaluation studies (e.g. the JESSICA country specific studies and the ex-ante evaluations of the JEREMIE programme) but in most cases (in so far as there has been any evaluation at all) it has been limited to the discussion of the instrument as part of a more generic annual report (e.g. the annual reports for JASPERS, NIF, WBIF, FEMIP etc.).

³ For further details of all the co-financing instruments, see Annex 1 Inventory.

Finally, there are those instruments which are very new and for which there is neither an evaluation study nor an annual report (e.g. the LGTT, ELENA and MARGUERITE fund).

Given the variable rigour of the existing evaluation studies, and the similarity of form which many of them take, we have here addressed only those which are of most relevance to the aims of this particular study, namely the general review of 'New Financial Instruments' along with the specific evaluation reports on the RSFF, CIP and JEREMIE. These studies are particularly helpful, both in revealing the strengths and potential problems with new financial instruments but also because they show the common inadequacies of the existing analysis in addressing the themes raised in the terms of reference of this study. The following provides a brief overview of the findings of those evaluation studies, and outlines the limitations of those evaluations in terms of the questions which this report now seeks to address.

3.3.1. The New Financial Instruments Implementation in 2009 Report

This report (CEC, 2010a) is a primarily factual document which offers a brief, yet informative, survey of eight of the key financial instruments which form a central component of this study: the CIP; RSFF: TTP; LGTT; JEREMIE; JASMINE; ELENA; MARGUERITE.

The report reviews each of these instruments in turn with coverage of the following:

- the structure and objectives of each instrument;
- implementation (which sets out the amount which has been committed from the EU budget to the instrument as a whole, the number of actions which have been undertaken and the total value of those actions);
- awareness (which sets out the strategies which have been undertaken to publicise the instrument for example in the form of awareness days or website presence and practical guides produced for stakeholders and beneficiaries);
- outlook (which encompasses both the viability of the instrument itself and the impact of the economic outlook so far as it effects that viability, with details offered of the existing pipeline of projects. This section also mentions whether or not any evaluation studies have been undertaken or commissioned thus far).

Given the brevity of the document it is perhaps inevitably lacking in detail but it does provide a useful overview of facts related to the existing instruments. There is, however, an absence of interpretative analysis within this document, which serves to simply list EU successes rather than to critically evaluate the importance of those successes and/or reveal any impediments to further success.

3.3.2. The RSFF Evaluations

Two evaluations have been undertaken of the RSFF - one by the EIB in April 2010 (EIB, 2010a) and one by a 'group of independent experts' (the Expert Group (EG)) who produced a draft interim report in July 2010 (Mann *et al.*, 2010). The scope of both of these reports is extensive, covering the scope of RSFF activity, the relevance of that activity, effectiveness, efficiency, management, coherence and project specific evaluations of delivery and impact in relation to the priorities of the EU as a whole.

The overall findings of both the EIB and EG reports is overwhelmingly positive as the following from the expert group's executive summary makes clear:

the EG considers the RSFF a uniquely innovative, demand driven instrument, successfully introduced in the research funding of the EU within FP7 and having dramatically expanded the financing for RDI. (Mann *et al.*, 2010, p.6)

The basis for these findings is based on the fact that during a period of economic and financial crisis (EIB, 2010a, p. vii; p.31; Mann, *et al.*, 2010, p.6; 10; 11-12) that the RSFF scheme disbursed its resources ahead of time - outlays reached 65% of the total targets at the mid-point of the scheme (i.e. by the end of 2009) as against an anticipated target of 50% (Mann, *et al.*, 2010 p.6; p.17). As these reports emphasise, this was particularly noteworthy given the unprecedented nature of the financial crisis which resulted in 'a dramatic decline in the availability of finance for private investment in the EU so that access to the finance for RDI investments became an even more urgent need' (Mann *et al.*, 2010, p.12).

The financial crisis thus, perhaps paradoxically, increased the impact of the RSFF as whilst it was initially conceived of as an instrument designed to deal with the 'structural needs of RDI financing, it also met anti-cyclical needs ... [as] a particularly welcome risk crisis instrument greatly "facilitating" access to private finance for R&D intensive companies in Europe when banks were becoming hesitant in taking on board such risky investments of their own' (Mann *et al.*, 2010, p.12). The favourable rates offered by the RSFF also overcame problems for potential borrowers who may otherwise have been reluctant to invest in R&D given that such investments are often the first casualties in periods of fiscal uncertainty.

The reports also emphasise that success can be seen in terms of the capacity of the RSFF to deliver successful projects, with 80% of those interviewed in the EIB evaluation study indicating 'that the RSFF loan was a catalyst for opening up the private loan market' (EIB, 2010a, p.10), so leveraging contributions from private financiers and government grant financiers that would otherwise not have been there (see also Mann, *et al.*, 2010, p.17) - the reports put the estimated leverage effect at 14, with a total of EUR 16.2 billion of investments in research by the end of 2009 (EIB, 2010a, p.v; Mann *et al.*, 2010, p.19-20; see also Annex 1 -Inventory).

The RSFF is a demand driven rather than supply driven instrument. This means that it is not allocated on the basis of quotas set by the Commission with disbursements targeted at particular regions or made to projects on the basis of specific priorities (EIB, 2010a, p.10; Mann *et al.*, 2010, p.6; 12; 23). Such a mechanism may have been expected to undermine the capacity of the RSFF to deliver specifically on the policy priorities of the EU. However, whilst it is the case that over 50% of RSFF approvals were to just 3 countries (Germany, Spain and Sweden) and that over 60% of project approvals were in two sectors (engineering/industry and life science) (EIB, 2010a, p.4), this still enabled the scheme to deliver on the EU's policy objectives in the area of innovation (Mann *et al.*, 2010, p.18-19), financial sustainability and environmental and social performance (EIB, 2010a, 26-8).

Overall, such was the perceived success of the scheme that the EG made a series of recommendations to accelerate the RSFF to build on its success. These are summarised as follows:

During the present project cycle (i.e. 2011-13)

- that the EC approves release of the second tranche of EUR 500 million of EU funding as specified in FP7's legal basis (Mann et al, 2010, p.7; p.48);
- that given market needs the RSFF should 'utilise part of the EU contribution within the present RSFF agreement as a first-loss piece' so that the EU contribution be used first to cover losses with the EIB contribution only called upon in the event of potential losses exceeding the EU contribution. The impact of this is that the instrument would effectively be adjusted to promote a higher degree of risk taking (Mann, et al, 2010, p.49);
- that given the success of the RSFF an additional EU contribution is made of up to EUR 500 million, taken not just from FP7 but from other areas of the budget with an underspend such as agriculture or the European Economic Recovery Plan (Mann, et al, 2010, p. 52);

For the future (i.e. 2014 and beyond)

In reflecting on the period beyond the present budgetary cycle, the EG made a number of recommendations designed to further expand the RSFF's scope (Mann et al, 2010, p.54-7):

- to expand the budget in 2014 with an EU contribution of 'no less than EUR 5 billion';
- to couple this expanded budget with a commitment to release the funds from the loans which are presently being repaid to this future RSFF instrument. 'Doing so will mean that in the long term, the RSFF funding part from the EC will gradually become more of a revolving fund' (Mann et al, 2010, p.54; p.55);
- that given the considerable sums available within the regions under the structural funds for innovation and research (EUR 86 billion has been earmarked for the period 2007-13) which are primarily allocated as grants on the basis of a supply-side mechanism, there is a need to complement the RSFF with a regional perspective which draws upon the existing JEREMIE programme (Mann, et al., 2010, p.57).

While the evaluation reports were overwhelmingly supportive of the achievements of the RSFF, there were also a number of issues for reflection raised by the two studies. Both the EG's and the EIB's evaluation studies emphasised that in its present form the RSFF had failed to adequately deliver a framework which reflected the needs of SMEs, with particular issues raised in terms of the bureaucratic nature of the application process and suggestions made that the RSFF was designed to offer provisioning which was too large in scale for most SMEs. As the EIB pointed out in its evaluation, 'RSFF does not seem to be the right instrument to address SMEs directly' (EIB, 2010a, p.14. See also Mann et al., 2010, p.7; 19; 25-7; 50).

While there was acknowledgement that there were other SME specific instruments in the EU, there was a sense that it could/should be a priority for the RSFF in the future to invoke mechanisms to better serve the SME sector. This was particularly emphasised given that the SME sector was more likely to deliver on the innovation element of the RSFF priorities for

'research, development and innovation', which was acknowledged as being less effectively delivered than the priorities of research and development as of the date of the studies' publication.

Reflecting the concerns of the SME sector, there was an acknowledgement that RSFF decision making - initially at least - had been too bureaucratic, with project decision times from application to disbursement at 30.1 months on average in 2007 (EIB, 2010a, p.35). This had fallen by 70% in 2009 to 9.1 months so reflecting a streamlining of internal decision making which could/should prove to address some of the concerns of beneficiaries (EIB, 2010a, p.30; p.33).

Related to this, the EIB evaluation in particular emphasised that the RSFF was a relatively costly instrument to administer which 'did not reflect real cost coverage' - total administrative costs per EUR million of loan signed for RSFF projects were 3.5 times the average for EIB loans as a whole (EIB, 2010a, p. 21).

Finally, there were a number of issues which are rather more difficult to resolve, revealing tensions which are common to the use of innovative financial instruments in general. The first of these centred on the tensions between visibility and transparency and the commercial need to respect confidentiality. This desire for an absence of transparency manifests itself in both the EIB's need for confidentiality in terms of its operational practices and procedures and the RSFF beneficiary companies desire to maintain confidentiality due to intellectual property rights considerations (EIB, 2010a, p.9). Such tensions clearly affect the capacity for scrutiny and the dissemination of best practice and pose potential challenges in terms of promoting positive visibility for the programme as a whole (Mann *et al.*, 2010, p.35).

In addition, reflecting the comments made above by the EG on the need to expand the EC contribution to the RSFF, the EIB has requested that the EU take on a greater role in terms of risk sharing. Without this, tensions will continue to exist at the heart of the RSFF in terms of the EIB's relatively low risk appetite (while it is taking on more risk it is doing so in 'a controlled and clear framework') and the EU's desire to use its budgetary contribution to 'maximise Risk Capital disbursements' in order to deliver high quality projects with real added value (Mann, *et al.*, 2010, p.34; EIB, 2010a, p.18). It is a desire to resolve such tensions that lies at the heart of the EG's recommendations set out above for an expansion of the EU contribution to the RSFF, which would be operated on a 'first loss piece' basis.

3.3.3. The CIP Evaluations

The CIP has undergone two different substantive evaluations: the Commission's annual implementation report (CEC, 2010b) and an expert group report commissioned by the EU to provide an evaluation of the CIP programme as a whole and to provide a more specific evaluation of the Entrepreneurship and Innovation Programme (EIP) of which the innovative financial instruments are a crucial part (GHK Consulting, 2010a; 2010b).

The Commission's report provides an audit of existing activity across the whole range of CIP activities (many of which are beyond the scope of this report). In terms of the specific focus here on innovative financial instruments, the report provides macro-level data which indicates the scale of support offered by the two key instruments during the period 2007 to 2009: the GIF has supported the creation of 18 VC funds in 15 countries, resulting in EUR 204.9 million of EU investments supporting 82 SMEs (CEC, 2010b, p.7); and the SMEG has resulted in 27 deals with financial intermediaries in 14 countries providing guarantees of EUR

195 million supporting over 64,000 loans to nearly 59,000 SMEs (CEC, 2010b, p.7). The remainder of the report provides a number of box out case studies which provide a number of 'positive examples' with testimonials of support from SMEs which have benefitted from EU investment and technical assistance (CEC, 2010b, p.7-9). Overall, therefore, this report is best seen as a promotion of present activity rather than an attempt to provide a systematic evaluation of the strengths and weaknesses of that activity as a whole.

In contrast the reports undertaken by GHK Consulting are a much more analytically based series of documents, comprising a review of the CIP framework programme as a whole (GHK Consulting 2010a) and more specifically of the Entrepreneurship and Innovation Programme (GHK, 2010b). While there is considerable overlap in the contents of these reports, both are briefly addressed here as their findings were important as a springboard for the fieldwork that was undertaken within this study.

Perhaps the most useful of these documents is the *Interim Evaluation of the Entrepreneurship and Innovation Programme* (GHK Consulting, 2010b) which provides considerable detail specifically on the financial instruments. Chapter 4 of the study is particularly useful - following a contextual discussion, which sets out the scope of activity under the different instruments (pp.31-2) and provides an overview of the theoretical debate on the nature of the problems confronting SMEs in terms of access to finance (p.35-40), it offers analysis of the financial instruments under the following themes: economic costs and benefits; implications for SME capacity building, and programme effectiveness (pp.31-75).

Economic costs and benefits

Reflecting the findings of the RSFF evaluations, the evaluation of the CIP finds that the financial instruments have delivered generally highly positive economic outcomes.

First, it reflects on the extent to which these instruments have caused potentially negative economic effects such as moral hazard or market distortion, finding that in both cases there is little evidence of such effects (2010b, pp. 41-3). In the case of market distortion, for example, this is limited in both the venture capital sector given the limited development of that sector and in the case of the SMEG loan guarantee facility due to the Commission's additionality rules which 'prevent intermediaries from substituting their own lending with European funds and encourage them to lend to segments not covered by the private sector' (GHK Consulting, 2010b, p.43).

Second, a number of positive economic effects are attributed to the CIP financial instruments in terms of the 'demonstration effect', job creation and financial leverage. In terms of the demonstration effect, which utilises publicly funded instruments to demonstrate that returns can be made from the market, there has been a particularly positive benefit in terms of the venture capital sector with the EU financial instruments playing a 'critical part in market-making' (p.44). In terms of job creation, similar benefits were found. Whilst the study acknowledged that precise estimates of job creation were methodologically problematic due to the nature of the monitoring instruments associated with the CIP programme (p.57), they overcame this by undertaking a combination of fieldwork in the form of an SME survey and drawing upon other sources of EU data in order to reach an estimate that nearly 300,000 jobs had been created or safeguarded in 234, 066 SMEs (p.58). Finally, positive economic benefits were recorded in terms of leverage, with leverage of 1: 6.5 estimated for the Venture Capital funds (meaning that 'every 1 EUR of EU investment generates 6.5 for SME financing') (p.63), while the leverage for loan guarantees was estimated at a total of 1: 67 for the SMEG instrument as a whole (i.e. every 1 EUR of EU investment generates 67 for SME

financing) (p.64). We return to discuss the methodological issues centred on estimates of leverage below.

SME Capacity Building

In general terms, positive results are also reported in terms of the importance of the financial instruments in terms of building SME capacity. In the case of the Venture Capital funds, the report argues that 'only one in 25 companies would have been set-up without the investment from EU backed VC funds' (p.60) and almost two out of three companies indicated 'that their company would not still be trading if they had not been successful in raising external equity via the ETF Start-up Facility' (p.71). Other positive benefits are seen in terms of the capacity of the programmes to aid the development of the fledgling 'business angel investment market', with the EIP seen as particularly effective in this regard (p.50).

In terms of the SMEG loan guarantee, the report's findings are generally positive but less equivocally so. The surveys reveal that whilst 43% of respondents reported that the SME loan guarantee was the only source of finance available to them, 34% revealed that they could have received the full amount of the loan from elsewhere but preferred the loan guarantee instrument (p.70). Given this finding, this leads the report's authors to surprisingly conclude that 'the utility of the SMEG loan guarantee was somewhat limited' (p.70). Yet the other interpretation of these findings is that the majority of SMEs in fact needed the loan guarantee in order to undertake their project. As the GHK report argues earlier, 'two out of three companies would not have undertaken the project without the guarantee loan (SMEG), or would have done less' (p.59). Overall, the relative benefits derived from these instruments are thus a key element in the recommendation that venture capital activity be a priority of the future development of CIP financial instruments (p.72).

Programme Effectiveness

Finally, the GHK Consulting evaluation offers insight into a number of issues which may be best labelled as programme effectiveness, covering the overall objectives of the programme, overlap between the CIP's objectives and other EU programmes, cost effectiveness and bureaucratic concerns in relation to the CIP instruments.

In terms of the overall objectives of the programme, the report reached the conclusion that the focus on the use of financial instruments is particularly appropriate given the generally held view within the literature that access to finance is crucial to enhancing competitiveness, which is a central aim of the programme (pp.45-8).

However, more mixed findings were reported in terms of the danger of overlap between the CIP's instruments and those being developed by other programmes, focused in particular on the JEREMIE scheme. While JEREMIE is regionally based and the CIP is a Community-wide instrument, the duplicate schemes pose 'practical difficulties' due to overlapping competences: the CIP instruments, like JEREMIE, have a potentially strong administrative role for the EIF; like the CIP instruments, JEREMIE is engaged in the provision of financial services such as loan guarantees and venture capital, and like the CIP instruments, JEREMIE is targeted at the SME sector (GHK Consulting, 2010b, p.53-4). Such concerns of overlapping policy jurisdictions are indicative of the broader concern of 'some Commission officials [that the] CIP lacks strategic focus and its objectives could be better specified' (GHK, 2010a, p.38).

Furthermore, while acknowledging that the CIP has proven to be particularly useful in terms of institutional capacity building for all states (GHK, 2010a, p.47), the report raises some concerns that the CIP is perceived to be 'less relevant' to the 'new' member states' SME sectors than it is to those of the 'old' member states. This is due to a combination of the relative inexperience of 'new' states in competing for resources, the market orientated nature of the instruments which may not suit their domestic levels of development and the inbuilt focus within the CIP on innovation which 'new' member states are less well equipped to benefit from given their relatively weak R&D sectors (GHK, 2010a, p.39).

In terms of cost effectiveness, the report is generally very positive about the CIP instruments: EIF fees are capped at market rates so maintaining value-for-money for the operation of the schemes (GHK, 2010b, p.66). Furthermore, cost effectiveness is de-facto enhanced for two interrelated reasons: the high rates of leverage recorded effectively reduce costs (GHK, 2010a, p.62) and there are strong reasons to believe that the majority of the money will be returned to the EU budget - it is possible that the whole Venture Capital budget could be returned and the amount allocated to cover losses under the guarantee operations has not been fully utilised, so suggesting that there may also be some returns here (GHK, 2010b, p.67-8).

Finally, the report was somewhat less complementary about issues related to the administration and bureaucracy surrounding the CIP financial instruments, with many SMEs complaining that the procedures required to access finance were overly complex and time consuming (GHK, 2010b, p.69). Related to this, and typical of many criticisms made of EU financial instruments in general, were issues related to visibility, with national stakeholders rating the programme as a whole and the associated financial instruments as generally weak in this regard (GHK, 2010a, p.66-8).

In concluding this discussion of the CIP financial instruments, it is important to briefly make mention of the impact of the financial crisis. Reflecting the RSFF evaluation set out above, the CIP evaluation is acutely conscious of the impact which the financial crisis has had on functioning of the programme as a whole. Yet whereas the RSFF had arguably benefitted from the financial crisis, the gains to the SME sector from the CIP are more precarious. As the report puts it: '[a]s regards the changes brought about by the financial instruments (such as businesses and jobs created; demonstration effect), their sustainability is likely to be affected in the current economic climate - given the broad macro-economic trends' (GHK Consulting, 2010b, p.72).

3.3.4. The JEREMIE evaluations

At present there is no systematic ex-post evaluation of the JEREMIE instrument comparable to those which have been undertaken of the RSFF or the CIP - and this in spite of the fact that the initiative was launched in October 2005, with EIF-JEREMIE mandates dating back to 2007 (EIF, 2009b, p.4; p.6). At present, the studies which have been undertaken consist of a series of *ex-ante* country and region specific studies designed to evaluate the extent to which JEREMIE could serve to address existing market needs and a summary of JEREMIE roll-out.

The first JEREMIE report, *Executive Summaries of Evaluation Studies on SME Access to Finance*, published in March 2009, provides the executive summaries of 53 country and region specific reports which were undertaken by the EIF in order to provide an ex-ante evaluation of the appropriate level of support which could be offered by the JEREMIE scheme to the SME sector (EIF, 2009a).

The evaluations were designed to identify gaps between existing levels of supply and demand for SME financing and make proposals for an appropriate balance of financial instruments which would fill those gaps (p.4). While acknowledging that there are a number of methodological challenges with such research, the EIF claim that confidence can be upheld in the findings on the 'basis of the EIF's wide experience of guarantee and equity instruments across Europe' which enable it to make proposals which 'reflect the standards of best practice in the market' (p.5).

The second key EIF report, *Progress Report on Evaluation and Implementation Activities in 27 EU Member States*, was published in July 2009 (EIF, 2009b) and provides an overview of the progress of the implementation of the JEREMIE scheme. Following the framework of the earlier ex-ante report on SME support (EIB, 2009a) the report provides a detailed description of the progress which has been made in each of the 53 countries/regions which were earlier examined in the region specific reports. What is perhaps the most striking finding is that only 9 of the 53 (subsequently increased to 11 of 53) regions/countries had at the time of the report's publication formally committed to the implementation of a JEREMIE scheme with the EIF acting as a holding fund manager (EIF, 2010a, p.32-4; EIF, 2010b, p.1). By November 2010, 30 holding funds had been set up with 11 managed by the EIF but the other 19 administered by other arrangements on the basis of the preferences of the managing authority, with a total of EUR 0.3 billion administered to SMEs via financial intermediaries (EIB, 2010b).

These reports thus provide a combination of a pre-implementation evaluation study designed to reveal market needs and a summary of the existing state of play with regards to JEREMIE implementation, rather than an *ex-post* evaluation of the extent to which the JEREMIE scheme has delivered on or satisfied those market needs: such research still needs to be undertaken following the flow through of sufficient funds to the final recipients (SMEs).

In reflecting on the evaluation studies of the financial instruments set out above there are a number of obvious strengths and weaknesses, as well as certain issues where the picture is more mixed. The remainder of this chapter offers a brief summary of those key themes in relation to the terms of reference as specified within this particular study and draws on our fieldwork findings and analysis in order to reveal both the extent to which the existing evaluations provide insight into those issues and their limitations in addressing the questions raised.

3.4. An Analysis of Co-Financing

This section sets out the fieldwork findings and analysis in relation to the implications of EIB and EBRD co-financing for the EU budget, with respect to the key issues raised within the terms of reference with reference to budgetary liability and management, governance and accountability, budgetary control, transparency and visibility.

3.4.1. Financial Liability

Does the development of co-financing pose greater threats to the EU budget in terms of financial liability?

There is little within the existing studies which suggests any cause for concern in relation to budgetary liability and budgetary control, albeit that this question is not really addressed directly. Instead, the studies emphasise the positive financial flows which have been generated by the programmes in terms of leverage etc (as discussed above).

The fieldwork analysis suggested that there were no specific concerns in terms of budgetary liability. All of the respondents were explicitly asked questions about the extent to which the development of co-financing and new financial instruments *within the EU* posed any additional risk to the budget in terms of budgetary liability (the discussion of the guarantee for the EIB's external lending activity is covered in Chapter 4). The conclusions were clear and unanimous - none of these instruments pose any formal risk to the budget due to the way that they have been designed. All involve allocations to programmes which are capped in size and none of them pose a risk to the budget beyond that which is initially committed. Even in those cases in which the financial instrument involves a form of guarantee (e.g. the LGTT and SMEG guarantee fund) there remains no liability beyond that which was originally committed during the design of the instrument. A discussion of the LGTT demonstrates this particularly clearly.

The LGTT is a guarantee instrument designed to aid the development of the TEN transport initiatives. It contains a joint contribution of EUR 500 million from EU budget and EUR 500 million from EIB, designed to be used as an insurance policy to insulate the developer of the project (e.g. a road scheme) against a lower than expected level of revenue due to lower than expected traffic volumes. The LGTT guarantee is sold to the developer effectively as an insurance premium based on the EIB's assessment of the risk associated with the traffic projections. If the projections prove to be accurate then there will be no call on the guarantee. If, however, traffic levels fall below those projected then depending on the nature of the agreement reached there may be calls on the guarantee. The limited risk to the budget is shown by the fact that even if the whole of the EU budgetary contribution is used up (for example if a number of LGTT guarantees were called upon) the instrument is designed such that the EIB would be liable to take all further losses. There is thus no extra vulnerability to the EU budget even in the event of excessive losses. The EIB's desire to mitigate against this situation should ensure an appropriate level of due diligence such that this eventuality is in practical terms a theoretical rather than an actual concern.

In the case of revolving funds, again there is no risk to the budget. In such cases, the aim is to place money into a fund, which while provisioned to undertake risky activity, assumes that profits will be generated from that activity which will revolve back into the fund. Interviewees acknowledged that such funds would require periodic replenishment but that this would be subject to the support of policy makers.

Thus none of the co-financing instruments which have been developed for activity within the EU pose any risk to the EU budget in a strictly financial sense - they all have capped liabilities and none sets potential losses against the EU budget.

While there are no theoretical liabilities to the budget, it is important to emphasise that there are, however, some financially related issues which should be borne in mind. As a number of the respondents pointed out, there is the potential for damage to 'reputational risk' which could come from 'some huge scandal', for example through fraudulent payments made by financial intermediaries within a co-financing environment. As we point out elsewhere in this chapter, co-financing poses particular challenges in terms of monitoring and transparency and thus poses potentially greater theoretical threats to 'reputational risk'. Possible challenges here could be from a Venture Capital fund manager, for example, who invests in

non-SME beneficiaries (non-qualifying companies) in spite of the fund being targeted at SMEs. Yet even here, the risks are largely theoretical - the EIF as the intermediary working on behalf of the EU has considerable capacity to exert moral pressure on the fund managers and ultimately to deny them access to future EU schemes. Thus even here the risk seems to be largely theoretical rather than actual, and overall there are few, if any risks, to the budget in terms of financial liability.

3.4.2. Budgetary Control

Are there any risks to the EU budget in terms of budgetary control which stem from the development of co-financing?

Questions of budgetary control are also absent from the existing analysis. The instrument specific nature of the evaluations perhaps precludes such analysis, given that they are focused within the instruments rather than on the controls which can be exercised by EU institutions over those instruments - interviewees approached for this report have thus been probed extensively on this issue.

The key concern here, which is touched upon elsewhere, is the extent to which the creation of innovative financial instruments makes the EP's job more difficult in terms of exercising budgetary control. While the EP is formally involved in the framing of these instruments, and in the decision to place parts of the budget at the disposal of financial intermediaries, so arguably maintaining formal levels of control, a number of challenges present themselves in terms of the arms-length nature of that control and the extent to which implementation becomes progressively detached from the operational influence of the Parliament and Commission. Fieldwork interviews raised a number of important issues which are central to a reflection on questions of budgetary control.

First, a number of interviewees suggested that in spite of the growth of co-financing budgetary control remains high as the decision to create such instruments rests with the Commission and the decision to allocate resources to them is subject to EP ratification. In relation to our suggestion that control may be a concern, as one respondent put it, 'Do not be so sceptical! Even if the power comes from the EIB, decisions still have to go through the Commission and the EP is now very powerful and has a say in every area of activity'.

Second, the nature of the instruments themselves were seen by some respondents as actually helping to maintain budgetary control. As was argued, a financial instrument where you have to pay back the loan creates discipline: the project sponsor has to demonstrate the quality of the project to the financial intermediary who will subject the project to intense scrutiny prior to lending the money. From this point of view, therefore, there is a level of control built into the very heart of the co-financing instrument as the 'selection mechanism which takes place ensures that there is safety in the system'.

Yet the nature of the instruments could also be seen as weakening budgetary control in the light of comments from a number of interviewees who suggested that an adherence to flexibility was crucial if co-financing is to work. As one of the respondents put it, 'historically there have been some excesses in control. Now over time this has changed. They [the Commission] are seeing that they cannot replicate their structures with us'. What is important here is that a desire for flexibility could potentially suggest a weakening of budgetary control.

Third, this theoretical concern with budgetary control was seen to vary from instrument to instrument. For example, the JEREMIE scheme has a variety of different Holding Fund structures in place with the EIF controlling about '1/3 of the pot whereas about 2/3rds is controlled by national institutions'. Associated with the Holding Fund structure are the regional banks and financial institutions who work on behalf of the Holding Fund to disperse the monies to the SME beneficiaries. Thus with a number of links in the chain, the potential for a weakening of budgetary control seems very real. As one respondent put it, 'we question whether the EIB can control the fund managers'.

However, it is important to emphasise that on this point there was considerable disagreement between the different interviewees about how genuine such concerns should be. Those who focused on the final end of the chain were generally concerned that co-financing was likely to reduce EP and Commission control, whereas those who focused on the first stage of the chain - i.e. the link between the Commission and the EIF - emphasised the robust framework for control. In particular, these latter respondents emphasised that the Commission has considerable knowledge of the Holding Fund structures and that while it is not centrally engaged in the details of the investment strategy, it has considerable control over the overall direction of the instrument through its involvement in the Investment Board, to which the EIF is accountable. Furthermore, making use of the EIF as a Holding Fund manager (where it takes on that role) has for some actually increased accountability and control, given that the alternative would be to place the management of the Holding Fund in the hands of the national or regional managing authority which would potentially loosen control still further.

The key point here is that questions of control are to a degree based on an evaluation of what the position would be without the co-financed instrument. In the case of JEREMIE, it is important to emphasise that the money would still be being dispersed via the managing authority, with associated implications for budgetary control - the creation of a Holding Fund structure which involves the EIF may well therefore enhance control. Yet in cases in which the co-financing instrument creates a framework that replaces directly administered grants, then control is necessarily sacrificed. Themes related to this are discussed further in the sections on 'transparency' and on the 'tensions between political and economic priorities'.

Overall, having evaluated all of the evidence from the desk research and the fieldwork interviews, our conclusions are that while the EP is formally involved in the framing of these instruments, and in the decision to place parts of the budget at the disposal of financial intermediaries, so maintaining high levels of control in the formal sense, a number of challenges do present themselves in terms of the arms-length nature of that control following the implementation of co-financing. In particular, we are of the view that control is inevitably reduced within a framework in which a financial instrument is run via an intermediary (such as the EIF) which then passes management of financial disbursement to a further intermediary (e.g. a bank).

Furthermore, budgetary control is also potentially reduced with the development of co-financing in terms of the relationship between the European Parliament and the implementing institutions. For example, while the Commission is formally accountable to the European Parliament for the implementation of EU policy, the control which the EP can exercise over either the EIB (which is owned by the member states) or the EBRD (where the EU has a very minor role in relation to governance) is much more limited. Yet this is an issue of greater relevance to policy evolution than it is a risk to budgetary control: it is thus addressed in terms of a more generic discussion of the relationship between the utilisation of the EIB and EBRD and the delivery of the objectives of the EU below.

3.4.3. EU Strategic Objectives

Does the use of innovative financial instruments compromise the EU in the delivery of its strategic priorities?

One key question raised by the terms of reference is the extent to which the development of innovative financial instruments makes it more difficult to gain a sense of the relative importance of various policy areas within the EU, and from that the strategic objectives of the EU as a whole.

It is not possible to discern the nature of the EU's strategic objectives from the analysis which presently exists of EU financial instruments: partly because of the limited number of evaluations which have presently been conducted, making it difficult to extrapolate from their findings, and partly because many of the principal areas of EU activity do not fall within the rubric of the existing financial instruments (e.g. the CAP, most of the structural funds activity, foreign and security policy etc). However, one key question which can be captured is 'do the instruments help to deliver on the objectives of the related policy area?' For example, the CIP has a key emphasis on competitiveness and the RSFF has a primary focus on research and innovation, both of which are strategic priorities for the EU as a whole.

In looking at the existing evaluation reports, the answer to this question is generally yes, but with some caveats. The evaluations make it clear that the financial instruments have been important in delivering on the priorities in the case of the RSFF and CIP, in particular in leveraging considerable sums to promote research and innovation and competitiveness and SME activity respectively. The findings of the evaluation reports in this regard were strongly corroborated by the interviews. Yet certain issues revealed by the existing evaluations suggest that there are some difficulties with these instruments in delivering on the EU's strategic objectives, even at the level of the policy objectives prescribed. These are particularly felt in terms of the uneven rollout seen, for example, in the absence of penetration of both the RSFF and CIP within the 'new' member states and in the uneven penetration of the RSFF to the SME sector. In addition, there is some concern that when taken in isolation the evaluation of an individual instrument may not reveal the effect of clashes with other instruments on the delivery of the strategic objectives of the EU as a whole (touched upon, for example, in the discussion of the overlap between JEREMIE and the CIP).

The overlap in competences and clashes between JEREMIE and the CIP were discussed at some length by a number of interviewees who almost universally shared the view that there was indeed a potential problem here, with respondents pointing to the duplication of function albeit with a fee structure which was '10 times the level of the CIP' for JEREMIE. There was some disagreement between interviewees about whether there was a justification for both instruments - supporters of retaining both argued that the CIP, while highly effective, was only useful 'to those with a culture of using such instruments', whereas JEREMIE was resource intensive because it filled a market niche in opening up markets which did not have an entrepreneurial culture and 'where the CIP had difficulties to go'; critics of having two instruments argued for an EU-wide framework and expressed concern that regional Venture Capital funds could actually 'torpedo' the viability of the CIP, suggesting that their track record has 'tended to be between poor and disastrous'. Finally, there was the view that the flexibility and duplication offered by JEREMIE could be seen as a temporary phenomenon, with states graduating to a standardised instrument when their economies and institutions had developed sufficiently.

Overall, therefore, even the question, 'is the EU delivering for the SME sector?', can only be partially answered with an instrument-by-instrument approach to evaluation. What is needed is a combination of a sectoral and macro-level approach in order to reflect upon the role of innovative financial instruments in the delivery of the overall strategic objectives of the EU, which is central to the aims of this study and the resulting fieldwork research, as we demonstrate here.

It is important to emphasise that there is a widespread desire to expand co-financing across the European Commission, EIB and EBRD. As part of the EU2020 process, interviewees frequently reported that there has been an increasing alignment of EU and Bank priorities (particularly with the EIB) to explore 'what products we can develop which deliver EU objectives'. Co-financing is thus seen by many as integral to progressing EU objectives, with a strong political will amongst most of those we spoke to 'drive this process'. As one respondent put it, 'the atmosphere is very favourable to financial instruments', particularly because there is a feeling that the 'EU budget could shrink' with co-financing seen as a way of 'channelling more money than in the past'. As another put it, 'with very little money you can trigger very big investments.'

EU Strategic Objectives: The Role of the Banks

Crucial to the consideration of the extent to which co-financing can actually deliver on the EU's objectives is a sense of the extent to which such objectives are aligned with those of the EIB and EBRD. At a formal level, the Commission is accountable to the European Parliament for the implementation of policy, yet the relationship with the banks is much looser. This was a theme which was also extensively explored with the interviewees.

We first explored the hypothesis that because co-financing with the banks is loan-driven, and loans are a demand driven instrument which require a borrower, this could well serve to reduce the capacity of the EU to deliver on its objectives, particularly if there was a mismatch between those objectives and the priorities of borrowers.

In response to this hypothesis, some of the interviewees did make it clear that there was a possibility of such an outcome - both the EIB and EBRD are banks which have to be able to find borrowers to lend to. A great deal of this lending is project lending and as one put it, 'we cannot force loans out of the door'. Given the importance of lending, there is thus a danger that the banks' activity could place bottom-up pressures which serve to shape the very proposals that the Commission is developing. There was also the view expressed, again by a minority, that the objectives of the EU were so broad that almost any lending could be seen as compatible with the EU's strategic objectives. However, the overwhelming view was to reject such positions, instead emphasising that lending, particularly in the EIB, is on the basis of guidelines which have to be approved with the Commission and member states. As one put it, 'the risk of non-alignment [in policy terms] is minimal because the Commission shapes the policy' and it can maintain influence over the banks by placing appropriate instruments in place (e.g. guarantees) to make lending more attractive to them.

We also explored the hypothesis that it was easier to deliver EU objectives in partnership with the EIB than it was to do so with the EBRD. Our contention is that such a view relies on overly simplistic caricatures of the differences between the banks which are politically motivated.

The first of such caricatures emphasises that the EIB is an 'instrument of the EU' whereas the EBRD is free from EU control, so that the EU can deliver its objectives through the EIB but can not do so through the EBRD. There were a number of respondents who did indeed articulate this view to us: as one put it, 'We are a very special bank. Compared to a bilateral or multi-lateral bank, we have no policy brief of our own. We are an instrument to implement policy which is made elsewhere. We do not have by mission the objective of implementing our own policy goals'. Thus, 'we see the EIB as an extension of the EU budget', and the EIB was seen as 'the bank of the EU'. Such accounts place emphasis on the statutory framework surrounding the EIB, and the fact that the 'treaty base defines our missions which is to support EU policies' which 'makes us special and different'. The implication was that in devising co-financing instruments the EU would be best able to realise its strategic objectives in working with the EIB as it was a 'natural partner' of the Union rather than working with other IFIs which have different rules and objectives.

We have some doubts about the accuracy of this account, on the basis that as a bank the EIB has a number of internal pressures which dilute the purity of its adherence to the EU's strategic objectives. On the one hand, a number of respondents emphasised that the EIB was only interested in 'volume lending' (i.e. to large scale, relatively low-risk projects) and was strongly driven by a framework in which cost recovery was instrumental to its internal processes. This suggested to us that there were some tensions between the EIB's role as a policy driven bank which may require increasing risk taking and its need for 'full cost recovery'. We return to this theme in Chapter 6.

The second caricature suggests that as a non-EU bank the EBRD will not be effective at delivering EU objectives. At a formal level, there is some basis for this view - as one respondent put it, whilst the EBRD is seen as a European Bank, 'the Commission cannot control us in the same way [as it can control the EIB]'. This can create situations in which the EBRD will proceed with a project which the EIB has been prevented from proceeding with for political reasons. In formal terms this difference stems from the fact that whilst the Commission 'enjoys veto rights on transactions within the EIB' it does not have any veto rights within the EBRD, 'with the EU being just one of 61 shareholders', and the EBRD having a very different mission to the EIB. These differences potentially profoundly affect the capacity of the EBRD to deliver the strategic objectives of the EU.

Once more we see this view as an overly simplistic one given the realities confronting the EBRD, which in fact enjoys close links to the EU and has a strong desire to deliver on EU objectives. The Commission is clearly able to exercise leverage over the EBRD through the creation of the platforms and policy instruments which govern its relations with it. As one respondent put it, 'there are huge areas in which we link up ... competition, transparency, governance, the environment etc.' Furthermore, there is considerable good will on behalf of the EBRD to seek better relations with the EU. As one interviewee argued, 'we want to have an excellent relationship with the EU so that the EP continues to support our work'. Finally, it is important to emphasise that there is a strong desire from within the Commission itself to work with a number of IFIs in order to help them to deliver the projects that they want to achieve, with a view that the more IFIs that are on board, the more likely it is that they will be able to deliver on their objectives. Grants, therefore, become key to lever in interest from the banks to get them to support the projects which are EU priorities.

EU Strategic Objectives: Case Studies

We suggest that the key way to ascertain whether or not co-financing helps the EU to deliver on its strategic objectives is to evaluate some specific examples. Here we focus on two key

issues: integrating the 'new' member states, and issues of transition in relation to future EU enlargement.

A particularly crucial strategic objective of the EU at present is to facilitate the economic development of the states which joined the EU in 2004 and 2007 (the so-called 'new' member states), with a central policy plank being the structural funds. Yet a number of respondents emphasised that as of the end of 2009 the rate of implementation of the structural funds stands at around 25% (against a target of 50%), with much lower levels in states such as Bulgaria and Romania. Three possible causes were identified for the low levels of absorption: the under-developed nature of the recipient economies, which lacked the state-led institutional capacity to develop strong projects alongside a lack of credit for the private sector; the impact of the financial and economic crisis, which had led to 'the first victim being the EU projects', and finally that the policy requirements of the structural funds were simply too complex and alien for the new states. Co-financing has been seen by a number of respondents as a key way in delivering on the strategic objective of raising structural funds absorption rates.

A number of interviewees discussed the importance of JASPERS, which is a technical assistance programme to help the new states deliver strong projects, in increasing structural funds absorption. As one respondent put it, when the countries became new member states decisions were passed to local ministries but while these ministries had 'lots of ideas they had no real implementation strategy ... we are now working more closely with more local authorities to implement these projects'.

JASPERS has been seen by many as instrumental to a programme of institutional capacity building at the national and regional level, but is also an acknowledgement that the EU has made mistakes in the structural funds roll-out to the new members: 'what is important is that we need to have well prepared projects otherwise there should be no funding. You could do other things but you can't have a discussion if there are no projects. JASPERS is crucial in helping in project preparation'.

The JASPERS framework is now 'fully established' with a pool of '80 or 90 consultants' and a 'EUR 30 million yearly budget' and was seen by a large number of interviewees as essential to structural funds absorption by linking project financiers to local municipal authorities and providing the technical assistance to develop well-formulated projects which would qualify for grants from the structural funds. These grants could be used alongside bank loans with the effect of delivering projects and so absorbing structural funds.

Overall, while JASPERS is seen as overwhelmingly successful there remain legitimate concerns that the considerable variation in the capacity of the 'new' member states to benefit from these instruments suggests that at present co-financing may be best suited to those markets which are relatively developed. This is particularly demonstrated with the ongoing and severe problems caused by both the financial crisis and the low levels of absorption of the structural funds in many of these states – problems which it is perhaps unrealistic to expect co-financing to overcome.

The second key strategic objective of the EU concerns transition and accession. Extensive discussion was held with the interviewees on the role of co-financing in this regard, with much of conversation centred on the Western Balkans Investment Framework (see Inventory, Annex 1) which 'has everything to do with the accession process'. Interviewees generally saw this as an excellent example of the potential offered by co-financing, arguing that after a period of inertia in the region in which there had been 'a struggle to find finance',

the co-financed contribution of just over EUR 180 million given in the form of grant money to aid project preparation had yielded project lending of over EUR 3 billion within a year. As one interviewee put it, 'with relatively little money you can trigger very big investments', with the framework successfully integrating disparate and uncoordinated activity. Respondents acknowledged that the needs of the region were such that it would be totally unrealistic to claim that co-financing could address all of those needs, instead emphasising that it had proven extremely beneficial in getting a number of projects off the ground.

Historically, 'different IFIs had been very uncoordinated' with 'huge amounts of money wasted'. The WBIF was seen as crucial to reversing this pattern, creating a 'one stop shop' which had been highly successful at bringing the IFIs together. As one respondent put it, 'there is not any real competition; the framework brings things together'. Prompted by engagement within the framework, the EBRD is frequently willing to use EU procurement laws and has been able to harness its expertise in delivering technical assistance through its personnel on the ground to complement the EU and EIB's desire for project-centred lending. As one respondent put it, the 'EU has been very positive in driving that process' with a view that the more that you can empower local governments to take over responsibility, the more you can help the accession process. EBRD interviewees were clear that 'we want to be part of that process', seeing substantial overlap between their focus on transition and the EU's emphasis on the instruments of accession.

Overall, in considering the issues in and around the role of co-financing and the delivery of the strategic objectives of the EU we are generally convinced that these instruments do indeed serve to help the EU in this way: many of the policy instruments are seen as highly successful, delivering projects which are compatible with the objectives of the EU. Yet there remain some issues of minor concern, centred in the uneven capacity of new member states to benefit from co-financing and what we see as an arguably unrealistic optimism about the capacity of such instruments to deliver in those sectors to which there is no obvious interest from a lender. Finally, it is worth remembering that co-financing remains tiny in scope and scale (little more than 1% of the EU budget is spent through such instruments) and that a great many EU objectives remain outside its scope. For example, when discussing with interviewees the scope of the instruments in terms of development work or small scale municipal projects in the field of energy efficiency, many spoke of the EIB as 'fantastically conservative', so suggesting that co-financing is unlikely to be the panacea for the delivery of many of the EU's objectives.

3.4.4. Transparency

How can the transparency of EU funds be guaranteed when these funds are subsumed in projects co-financed and run by the EIB and EBRD?

To a degree the act of audit and evaluation performed within the existing studies is designed to address questions of transparency - most of these studies make clear the scale of allocations from the EU budget and many also provide overviews of governance mechanisms etc. But in terms of monitoring the usage of EU funds, there is a problematic absence of detail as to how these programmes actually deliver on the ground. Critical evaluation of such projects, and hence of transparency, is essentially absent: the existing reports tend to be overwhelmingly self congratulatory, providing lists of 'successful' beneficiaries of the schemes (given in the form of box outs). There is thus a need for a systematic qualitative evaluation of the strengths and weaknesses of the use of co-financing, based on extensive fieldwork which is designed to offer critical reflection. Clearly such work is beyond the scope of a study

such as this but where appropriate insights have been raised by our fieldwork interviews these are set out below.

The critical point, which is raised by the EIB evaluation of the RSFF, is the tension which is presently at the heart of many of these instruments between transparency and the need for confidentiality in order to promote commercial activity. To varying degrees, this tension is germane to all of the innovative financial instruments in that the EU's desire for transparency, when working alongside financial intermediaries who are making lending decisions in a commercial context, must inevitably create friction.

Questions of transparency are central to the aims of this report, and are addressed to a considerable degree by the inventory, which sets out in detail the scope and scale of EU budgetary activity across the whole range of co-financed instruments. Such questions were also addressed through the fieldwork interviews, which reflected upon two key questions: how to gain a better sense of policy successes and failures on the ground, and how to balance the needs/desires of a commercial partner for confidentiality with the European Parliament's desire for transparency?

Our overall assessment in terms of transparency is that the EP is right to be concerned that co-financing poses particular challenges in this area, given a combination of the restrictions imposed upon the Court of Auditor's auditing and monitoring role and particular issues which are inherent in the instruments themselves.

First, the interviewees raised a number of important issues in relation to the capacity for monitoring in the EU. Restrictions presently exist on the capacity of the Court of Auditors to adequately monitor co-financing due to its mandate being restricted to 'the money which is from the EU budget'. Thus even in a blended or co-financed instrument the court is 'bound by statute and treaty by EU objectives' and it has 'no access to bilaterals' or EIB project financing, being able to audit only the element 'with Commission involvement'.

The existing process, as communicated to us by multiple interviewees, is heavily dependent on the Commission effectively exercising its responsibility to 'check if the money is being spent appropriately'. In the case of innovative financial instruments, which may involve national, regional and other intermediary organisations, many respondents expressed concern as to the capacity of Commission to exercise its monitoring function adequately. This thus places considerable pressure on the Commission to have robust processes for intermediary audit, in a context of general capacity pressures on its work; earlier reports by the Court of Auditors, for example on the MEDA, have revealed major concerns in terms of the monitoring of those projects being run by the Commission and the Banks.

There were two other concerns raised by the interviewees about transparency in relation to co-financing. The first was linked to the sheer complexity of these instruments which involve multiple partners, instruments and frameworks, leading one respondent to describe the audit trail as a 'nightmare!' With a duplication of collaborators comes a duplication of potential auditors - EU, national, local and sector specific - all of which serves to further raise questions in terms of transparency. It is a desire to secure greater transparency which lead to a number of interviewees advocating a framework of standardisation so generating 'consistency and coherent governance'. We return to the theme of simplification and standardisation in Chapter 6.

The second concern relates to the tensions which exist at the heart of co-financing between the EU's desire for openness and transparency and the desire of the banks for commercial

confidentiality. This was a theme which was raised in the RSFF evaluation discussed earlier and was one on which many respondents commented. From the point of view of the banking sector, the view was universally expressed that robust auditing mechanisms, undertaken by the appropriate banking authorities, were already in place, thus precluding the need for EU audit. In contrast, those outside the banks tended to take a very different view, arguing that the bank's stated desire for confidentiality in much of its operations raised considerable problems for transparency in a context in which public money is being blended with money from policy driven banks alongside potential private partners. We see this as a major tension which resides at the heart of the co-financing model and we remain of the view that there needs to be a serious investigation of the sustainability of a model in which the European Court of Auditors is restricted in its capacity to adequately audit the whole package of co-financing.

To this end we are encouraged by two reports which we note that the European Court of Auditors is due to publish in 2011 as mentioned in its work programme (CoA, 2011) in which it will undertake an audit of SMEG guarantee facility 'to establish whether the SME guarantee facility has been managed effectively' (p.15) and provide an audit of financial engineering 'to establish if the ERDF financial engineering measures add value and improve SME access to finance' (p.11). We see both of these reports as a highly welcome development but remain concerned as to how the Court will truly be able to address questions of transparency given the proliferation of private entities within these instruments. As one respondent put it, 'the CoA has no mandate to look at these private entities' and so is left with trying to see 'how can we best ensure that there are accountability mechanisms from these states', and thus of EU co-financing of the SME sector as a whole. We share the concern of many of the respondents as to the adequacy of this approach.

3.4.5. Visibility

Is visibility low in the case of co-financing and if so what can be done to address it?

At the heart of concerns about visibility is a desire to ensure that beneficiaries of EU budget monies are aware that the money has come from the EU. In spite of a consistent pattern in which the EU has actively sought to develop schemes to enhance visibility, all of the existing evaluation studies discussed above have found that stakeholder awareness of the EC contribution is limited. There is little awareness of the EU's role in facilitating these schemes, let alone appreciation of EU added value for example in the form of job creation, capacity building or financial leverage. Perhaps surprisingly, this absence of visibility even occurs in cases where important benefits for institutional capacity building have been attributed to the programme concerned.

In terms of the findings from the fieldwork, visibility was not a topic which engendered much discussion from respondents, but those who did address the topic raised some important issues in this regard. Interviewees saw visibility as quite distinct from transparency, with visibility being centred on knowledge of the importance of the EU's role in the facilitation of co-financing, whereas transparency is centred on the openness of the policy making system to external scrutiny.

The respondents who expressed a view on the visibility issue all agreed with the existing evaluations that visibility is a problem. The visibility issue was described as 'massive' and being 'very important to us', with respondents frequently frustrated that visibility amongst beneficiaries is very low. While there was an acknowledgement that there may be an

irreconcilable tension between transparency and policy effectiveness due to the complexity of these instruments (see above), interviewees did not feel that this should affect visibility.

The practical implication of poor visibility is that policies which are seen as highly successful from the policymakers' perspective have not resonated effectively, so reducing the perceived importance of the EU's role in facilitating that success. The cumulative perception amongst interviewees was that higher levels of EU visibility would help place pressure for an expansion of the scope and scale of policies facilitated through co-financing, something which they saw as a desirable development.

However, there was an acknowledgment that the multiplication of schemes in areas such as micro-finance (where there were 'four or five') and in energy efficiency (where there were also 'four or five') may paradoxically serve to reduce political and market visibility. This is because the competition between DGs, who were seen by some as rushing to promote their own particular co-financing initiative, would have the effect of creating duplication and ultimately confusion at the beneficiary level.

Of greater concern to a number of interviewees was what one might term inter-institutional visibility, which is a theme which has not been discussed in any of the present evaluation studies. In particular, a considerable number of interviewees felt that the growth of co-financing raised issues in terms of a lack of awareness within the EU institutions themselves about what was going on. This is quite distinct from concerns about transparency as we have argued earlier. In terms of the visibility of the banks, there was a strong feeling within both the EBRD and Commission that there was a low awareness of the EBRD across the EU as a whole, with a poor sense of how it differed from the EIB in terms of its methods of work, mission, areas of operation etc. Respondents felt that the EBRD was often perceived in terms of caricatures - i.e. as more expensive or engaged in small scale projects - 'if they know about it at all'.

For some respondents, the solution was for the EBRD to 'up its game' with a more active form of political participation, possibly through a permanent Brussels-based office specifically designed to increase its own visibility. This would also have the benefit of enhancing the visibility of co-financing more generally, and through that would have positive implications for transparency (see the discussion in this chapter elsewhere). However, other respondents emphasised that while the EBRD was less visible than the EIB, perhaps inevitably given that the EIB was often seen as the 'bank of the EU', this did not necessarily pose major operational problems. Day-to-day links between policy makers within the Commission, EIB and the EBRD are generally seen as strong, although frequently contingent on personal ties. Thus visibility at the policy-making level is considerably greater than it has been historically and there is strong knowledge amongst those who 'need to know' of the differences between the banks in terms of their modes of operation and areas of specialism. Yet this has not filtered through into the wider policy community either at a Commission DG level nor into the broader Brussels policy community. This is clearly problematic in terms of visibility for the EBRD specifically but also has the effect of reducing the visibility of co-financing more generally.

Poor visibility was not just a concern in relation to the EBRD, however, and there was a strong view from almost all interviewees that there was relatively poor visibility for the work of the banks in general. There were two possible implications to be drawn from this.

First, that there is a need for the banks to pro-actively increase levels of knowledge about what they are doing. Yet we have some doubts that this is the key problem - at present, both

the EIB and EBRD provide considerable information which is freely available on their website in the form of annual reports and of lists all of the projects which they have approved. This information is subdivided by sector, geographical region etc. and provides considerable detail about the nature of the project and the size of the loan disbursed by the respective bank. Thus it could be argued that the banks are in fact highly visible in terms of their project loans. However, in terms of the specific issues raised within this study, it is true to say that it remains difficult to ascertain specific details in the areas of co-financing. The nature of the loans which have been specifically granted under the EU's co-financing instruments are often unclear and the banks could arguably do more to clearly disaggregate the scope and scale of such activity. At a purely practical level, it was a highly challenging task for us to compile the inventory, and whilst we are incredibly grateful for the assistance offered by both the EIB and EBRD in this task, if they wish to enhance visibility in relation to co-financing then all of this information needs to be gathered into one place to provide a clear picture of the cumulative importance of co-financing.

The other possible implication of the 'poor visibility' of the banks, as expressed by a number of respondents across the Banks and Commission, was that this issue reflected less on the banks' provision of information and publicity and more on the need for the European Parliament, in particular, to do more to inform itself: the problem of visibility was more illusory than real. A number of respondents felt that the information was in fact available but that EU policy makers were simply 'not looking for it!' leading to considerable variation in the knowledge of parliamentarians in particular. This is not a trivial problem: there was concern that this was leading to some inappropriate and impulsive suggestions in terms of the policy debate on co-financing, with a lack of understanding of areas of crucial importance.

3.4.6. Political vs Financial Considerations

What are the political and financial considerations of the use of innovative financial instruments? Is there a trade-off between them?

Overall, the existing studies offer a number of important insights in terms of 'financial considerations' but they are rather more limited on the 'political considerations'. We addressed this imbalance within our fieldwork research as set out below.

In terms of 'financial considerations', the existing studies offer considerable insight into the financial benefits of the instruments, setting out the financial flows and gains from leverage and making it clear that the instruments address key market needs and do not distort the market. Furthermore, the evaluations make it clear that those instruments which are devised on a revolving nature, with sustainability and revenue generation embedded within their framework (such as the VC funds), are successfully delivering on those aims such that the EU contribution will be reimbursed to the budget. Even those instruments which might be expected to be drawn down, such as the SMEG loan guarantee, are likely to deliver returns to the budget, because the guarantees have not been fully called upon. Thus overall, the financial considerations reveal a consistent pattern of high financial deliverability with limited financial concerns for the EU budget.

Fieldwork respondents offered views which were consistent with those within the present evaluations in terms of financial considerations. Respondents offered multiple examples and made frequent reference to the high levels of leverage which had been seen through co-financing; emphasised the benefits which would flow from revolving funds in terms of

economic capacity building; made reference to the value-added which could come from EU involvement in projects, with for example the EIF seen as offering a 'quality standard' which 'would enable smaller investors to say yes' because they would trust the EIF to undertake due diligence; and placed emphasis on the way in which co-financing could be instrumental in market-building through the presence of financial intermediaries and the EIB and EBRD. As one respondent put it, 'we develop the market. We create the structure. We strengthen the credit analysis ... we helped to build up the financial sectors. There are many ways in which we push the market'.

The fieldwork was also important in revealing some potential problems with the existing financial evaluations and of the economic benefits more generally, although it is important to emphasise that such views were held by a minority of the respondents. Firstly, some concern was expressed that a desire to secure high leverage numbers may be itself politically motivated. In discussion of the ELENA instrument, for example, the view was expressed that the Commission's political desire to secure very high leverage figures had led them to channel all of the resources through the EIB. With the money primarily flowing to 'rich cities' it was seen as easy to achieve high leverage whereas 'genuine development work' would achieve much lower leverage. Furthermore, estimates of leverage need to be 'looked at with some caution' because the claims made hinge on the assumption that without the EU contribution that there would have been no alternative source of finance, which may be untrue. Secondly, some commentators emphasised that the predominance of the grant element, particularly in the case of the structural funds, could actually serve to make co-financing unattractive from the point of view of the lender: grants of up to 85% leave 'very little room for co-financing' and 'the fact that so much grant funding is available acts as a strong disincentive to the private sector'.

What the evaluation reports are somewhat less explicit in doing is making judgements about the political implications which stem from these instruments. There is some comment made about institutional capacity building and the excessively bureaucratic nature of these instruments, but the only substantive political issues which are touched upon are those to do with visibility (see discussion above).

The fieldwork interviews raised a number of issues in terms of the political implications of co-financing. The analysis offered here is necessarily thin as we just cover those themes which have not been addressed earlier in this chapter, many of which are also by implication 'political'. Like the published evaluations, the fieldwork interviews also placed particular emphasis on the positive role which co-financing could play in terms of institutional capacity building which could be facilitated by technical assistance, so enabling 'the beneficiaries to be involved'. Also on the positive side, interviewees pointed to the growing importance of the formal inter-institutional linkages which are occurring between the EIB, in particular, and the EU institutions. Respondents pointed to the fact that 'the EIB is now appearing at the EP increasingly frequently' and that there is 'a huge effort of the [EIB] presidency to inform the EP' of the Bank's operations. The EIB is thus itself becoming more politically engaged - which we contend is an inevitable, and desirable, outcome of the growth of co-financing.

However the fieldwork interviews also revealed a number of concerns in relation to 'political considerations' (again, the issues covered here are those which have not been addressed elsewhere). In addition to the key issues in relation to governance, visibility and control, some concerns were expressed that co-financing had led to some confusion within DGs as to how best to work with the banks. One bank for example reported that when trying to suggest working on a form of blended instrument within the energy sector the recipient DG had raised concerns that having a grant component might make the instrument fall foul of

state aid rules. In short, confusion as to how to square the implications of co-financing alongside the existing EU legal framework may well be an issue which leads to some reluctance amongst EU policy makers to proceed with such instruments. Co-financing raised similar concerns about jurisdictional confusion when dealing with sub-national and national actors and governments. For banks trying to work with national authorities, co-financing can throw up a myriad of local rules and regulations presented as questions of 'national sensitivity, legal obstacles etc'. Thus the very variety of the EU's political landscape may make co-financing politically problematic.

Overall, in reflecting on the question of the political considerations of co-financing in light of the analysis offered within the report as a whole, the central question is the extent to which these instruments reduce levels of political control either because the jurisdictional boundaries in relation to governance become less clearly defined or because the use of innovative financial instruments changes the nature of the formal relationship between the European Parliament and the disburser of the funds. For example, while the Commission is formally accountable to the European Parliament for the implementation of EU policy, the EIB is owned by the member states and is accountable to a governing board which is composed of Member State representatives. Similarly, the formal control which can be exercised by the Parliament over the EBRD is more limited as the European Community is only one member of the governing body of the EBRD. Thus a key question is how much impact does this have on the control which the EP has over governance in relation to the disbursement of funds when working with financial intermediaries? We would suggest that the answer to this question can best be reached through consideration of the above analysis.

Finally, it may be expected that the development of innovative financial instruments will involve a trade-off between increased financial benefits and a reduction in political control, such that policy makers would need to decide how to strike the right balance between these. We agree with this but contend that the conclusion as to how to strike this balance is best reached by the reader rather than the writers of this report. The arguments set out above provide material for deliberation on this question; we remain of the view that how such evidence is considered will to a degree be a matter of political judgement.

4. EU BUDGET GUARANTEES

This chapter examines guarantees extended by the EU that could make a call on the EU budget. The first section considers guarantees for 'indirect lending' (guarantees to the EIB for EIB lending to third countries). The second section looks at EU budget guarantees for 'direct lending' (loans extended to Member States). Each separate form of guarantee instrument is described – including its application and method of operation – before the implications for the EU budget are explained.

4.1. Guarantee of EIB Loans

Under the External Lending Mandate, the EU extends a guarantee to the EIB for operations in non-EU countries. The aim is to enable the EIB to undertake such operations (which often bear a significantly higher level of risk than the Bank's activities within the EU) at attractive lending rates without impacting on its 'AAA' credit rating. The guarantee covers both EIB loans and loan guarantees. It comprehensively covers the bank for losses on operations with the public sector (or public sector guaranteed operations) and for operations falling outside the public sphere (political risk only). In 2009, out of total EIB financing of EUR 79 billion, EIB activity outside the EU amounted to EUR 9 billion, EUR 6 billion of which was covered by the guarantee. The remaining EUR 3 billion represents EIB 'own risk' lending – typically lending to investment-grade countries and investment-grade structures in non-investment grade countries.

The EIB's guaranteed lending is supported by a guarantee fund (the Guarantee Fund for External Actions). The Fund was established in 1994 – at a time when guarantees to loans granted to non-member countries were rapidly growing – to cover defaults on loans and loan guarantees granted to non-Member States or for projects in non-Member States. The Fund (a) provides a liquidity cushion in order to avoid calling on the EU Budget every time a default or late payment on a guaranteed loan arises, and (b) creates an instrument of budgetary discipline – a limitation – by establishing a financial framework for the development of EU policy on guarantees for Commission and EIB loans to non-member countries.

A special provisioning mechanism is used to 'smooth' the management of contributions from the EU budget to the Fund. If, as a result of defaults, the activation of guarantees during one year ($n - 1$) exceeds EUR 100 million, the amount exceeding EUR 100 million is paid back into the fund in annual tranches starting in the year $n + 1$ (and continuing over subsequent years until full repayment).

Although the focus of this report is on EIB activity, the Fund actually covers three different instruments (each of which benefit from an EU budget guarantee):

- EIB lending in non-Member States (in support of the EU's external policy objectives);
- Euratom loans (loans to finance projects for improving nuclear safety in certain non-Member States – including the dismantling of nuclear power stations that cannot be upgraded);

- Macro-Financial Assistance (to non-Member States; essentially balance of payments support to enlargement and neighbouring third countries).

As Table 3 demonstrates, the largest instrument – by far – is represented by the EIB lending activity.

Table 3: The Community Guarantee Fund (at end-2009)

OUTSTANDING AMOUNT OF LOANS TO THIRD COUNTRIES	AMOUNT EUR MILLION (%)
EIB Lending in Non-Member States	15,810 (96.6%)
Euratom Loans	54 (0.4%)
Macro-Financial Assistance (to non-MS)	497 (3.0%)
Total	16,361 (100%)

Source: Report from the Commission to the Council and the European Parliament on Guarantees Covered by the General Budget, Situation at 31 December 2009, European Commission, 2010.

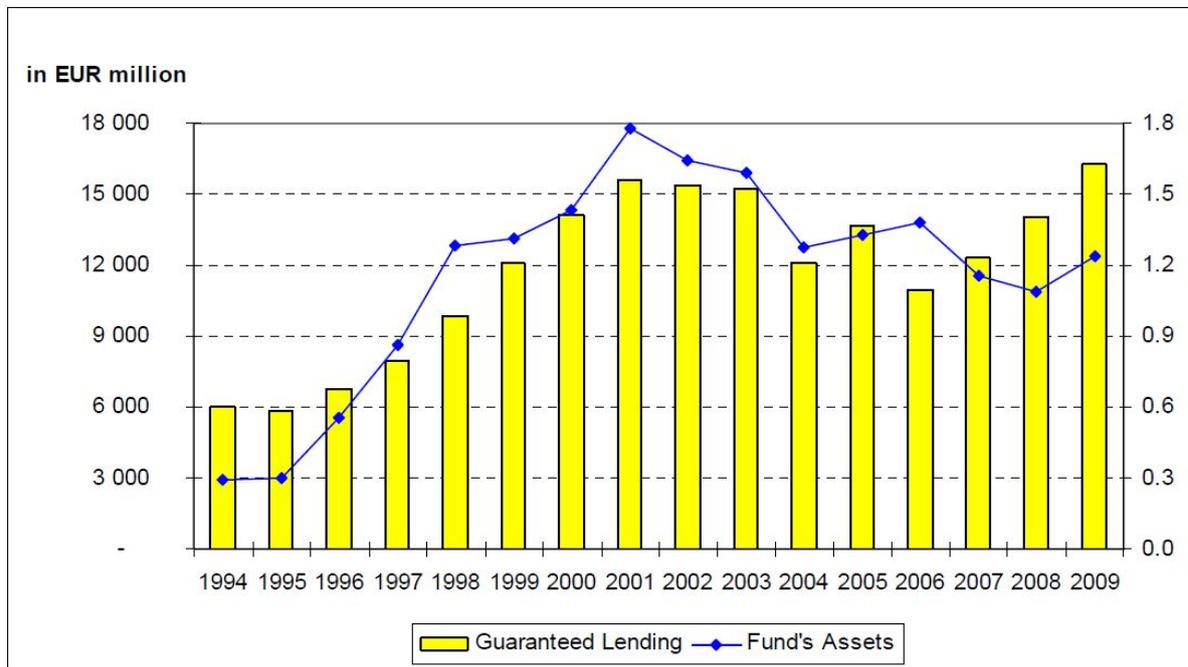
Note: Amounts include interest accrued.

Financing of the Fund is ensured from the general budget of the EU. The provisioning amount is calculated in any financial year based on the net disbursements of guaranteed loans granted during the previous financial year. Thus there is a lag of approximately one year between the time when amounts become outstanding and the actual provisioning of the fund. There is also a lag in the execution of the EIB mandate. The loans signed between a beneficiary and the EIB are not automatically disbursed the same year. The loans may be disbursed over several years and, in practice, may be subject to unforeseen delays. To avoid a lack of visibility with regard to when obligations might actually crystallise, a limit of 7 years has been established. EIB loans should be disbursed within 7 years from the end of the respective mandate (in this case, the 2007-13 mandate).

Financial management of the Fund is handled by the EIB (MFA and Euratom loans are managed directly by the Commission). The Fund is sized at 9% (the 'target rate' – see Figure 4) of all outstanding loans and loan guarantees (plus unpaid interest due). The 9% acts as a cash buffer; a 'shock absorber' for the Budget. Recently, the External Lending Mandate's lending ceiling was increased by EUR 2 billion (from EUR 25.8 billion to EUR 27.8 billion for the period 2007-13). All things being equal, to keep the Fund provisioned up to its 9% target, this would have a budgetary impact (ie. would require a transfer of additional amount to the budget item for payments to the Fund). However whether the budget is called or not depends on actual lending levels for all qualifying loans and on the level of default.

With resources of EUR 1.33 billion (31st December 2009) set against guaranteed lending (outstanding capital liabilities including accrued interest) of EUR 16.36 billion, the provisioning ratio stood at 8.15% (below the 9% target). For this reason a provisioning of EUR 138.9 million was paid from the Budget to the Fund in early 2011.

Figure 4: Provisioning in the Guarantee Fund for External Actions



Source: Commission Staff Working Document accompanying the Report from the Commission to the Council and the European Parliament (Comprehensive Report on the Functioning of the Guarantee Fund), COM(2010)418, European Commission, 2010.

According to the draft EU budget for 2011, provisioning of the Guarantee Fund amounted to EUR 93.8 million in 2010 and EUR 138.9 million in 2011, and could rise to EUR 200 million for the remainder of the current financial perspective (2012 & 2013). This anticipates strong external mandate activity in terms of the volume of signatures and amounts of loans disbursed. Although the figure of EUR 200 million is specifically identified, in reality the requirement is to set aside the amount needed to cover any shortfall between the 9% (ie. 9% times the outstanding amounts of loans and loan guarantees) minus the amount that is already in the Fund. If the Fund has sufficient resources, no Budget payments are required (no payments were made in 2007, 2008 and 2009 for this reason) – however, as mentioned above, a payment of EUR 93.8 million was required in 2010.

The EU guarantee is restricted to 65% of the aggregate amount of credits disbursed and guarantees provided under EIB financing operations, less amounts reimbursed and plus all related sums, with a maximum ceiling of EUR 27.8 billion (the revised External Lending Mandate’s lending ceiling for 2007-13). In terms of restricting the risk to the Budget, the 65% places a limitation on the EU guarantee given to the EIB for financing operations with non-Member States.

4.2. Guarantee of Loans to Member States

The EU budget also provides guarantees for loans to Member States under (a) the medium-term financial assistance for non-Euro area Member States' balance of payments facility, and (b) the newly created (May 2010) European Financial Stabilisation Mechanism (EFSM). The balance of payments facility is available to those Member States which have not adopted the Euro and are experiencing external payment difficulties. The Stabilisation Mechanism (EFSM) – established in the wake of the recent financial crisis in Greece – provides loans or credit lines to Member States (including EMU members) experiencing severe economic or financial distress caused by exceptional occurrences beyond their control. The Mechanism is expected to be a temporary facility; staying in place only as long as it is needed.

However, unlike the guarantees discussed earlier (for which a specific provisioning fund is established) the guarantees described here remain unfunded. As explained later, a margin ('headroom') is provided for in the EU Budget each year to cover guaranteed reimbursements. The guarantees themselves have no impact on the EU budget except in the event of loan default (in which case resources from the EU budget would be needed to reimburse the creditor).

Under the balance of payments facility, the EU budget can provide guarantees for loans up to EUR 50 billion. The EFSM – part of a EUR 750 billion package of measures designed to preserve financial stability in Europe – allows for EUR 60 billion worth of loans; again guaranteed by the EU budget. The two instruments therefore, together, provide for loans up to EUR 110 billion. As back-to-back loans – not grants – there is an expectation of repayment. Therefore, as mentioned above, only the event of default would have a budgetary impact and, to date, previous loans (to France, Greece and Italy, for example) were all repaid in full. At present, up to EUR 14.6 billion is allocated to Hungary, Romania and Latvia; leaving EUR 35.4 billion available under the balance of payments facility.

In terms of guarantees of loans to Member States, the risk borne by the EU Budget derives from the outstanding amount of capital and interest in respect of guaranteed operations. These are summarised (as at end-2009) in Table 4. For completeness – and for comparison purposes – operations covered by the Guarantee Fund (i.e. in non-Member States) are also presented.

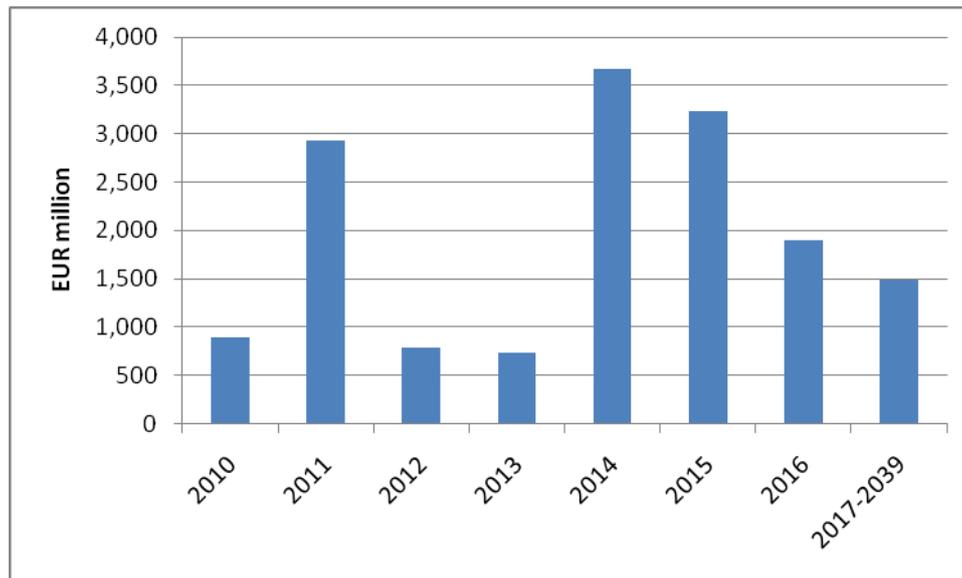
Table 4: Total Guaranteed Amounts Outstanding (end-2009)

FACILITY	PROVISIONING	OUTSTANDING (EUR M)	%
<i>Member States</i>			
BoP	Budget	9,304	31.3%
MFA		90	0.3%
Euratom		430	1.4%
EIB		3,570	12.0%
Sub-total		13,394	45%
<i>Non-Member States</i>			
MFA	CGF	497	1.7%
Euratom		54	0.2%
EIB		15,810	53.1%
Sub-total		16,361	55%
Total		29,755	100%

Source: Report from the Commission to the Council and the European Parliament on Guarantees Covered by the General Budget, Situation at 31 December 2009, European Commission, 2010.

As can be seen from Table 4, 55% of the total outstanding amount guaranteed is linked to third countries. The remaining 45% is for balance of payment loans and loans to (or for the benefit of) projects in Member States. A large proportion of the latter results from (a) the enlargement rounds (once a country becomes a Member State, the risk on the loans – eg. EIB loans – is transferred from the Guarantee Fund to the Budget), and (b) activation of the EU medium-term financial assistance facility for non-Euro Member States (the Balance of Payment facility).

At the beginning of 2010, the Budget was exposed to a maximum risk (linked to Member States) of EUR 890.1 million. This represents the amounts due in 2010 and assumes – reasonably (based on past experience) – that defaulting loans would not accelerate. Over 50% of this risk relates to exposures in Romania and Hungary. This EUR 890.1 million represents 36% of the total Budget coverage in 2010 (EUR 2.465 billion). The Member State-related budget exposure for 2010 and subsequent years is presented in Figure 5.

Figure 5: Annual Risk (Linked to Member States) Borne by the EU Budget

Source: Commission Staff Working Document accompanying the Report from the Commission to the European Parliament and the Council on Guarantees Covered by the General Budget, COM(2010)580, European Commission, 2010.

4.3. Budgetary Management

4.3.1. Guarantee of EIB Loans

As stated earlier, the annual budgetary resources available for provisioning the Guarantee Fund are EUR 200 million. The Guarantee Fund itself places an important and effective constraint (and control) on the amount of EIB external lending and guaranteeing. Together, the budgetary resources, the target rate and the experienced level of default combine to determine the maximum level of external lending that can be extended by the EIB. In truth, the annual allocation of EUR 200 million over the seven years of this Financial Perspective (a total of EUR 1.4 billion) is well in excess of the provisioning required to cover the associated liabilities.

In March 2010, an independent evaluation of the Guarantee Fund was published (GHK, 2010c). The evaluation involved desk research, interviews and quantitative analysis – extensive risk modelling using Monte Carlo simulation to (a) statistically examine the likely calls to the Fund, and (b) assess the ability of the smoothing mechanism to cope with these calls.

In summary, the review concluded very positively that:

- The Fund was an effective and efficient mechanism for provisioning for the risks associated with the EU's external lending actions, and it should continue to operate.
- Since 1994, calls for a total of EUR 478 million had been handled through the Fund (for defaulted EIB loans in the former Yugoslavia and Argentina). Net transfers from the EU Budget to the Fund had been EUR 484 million. Thus, over 15 years,

the cost to the Budget of operating the Fund had been EUR 6 million. The review commented that “these costs are modest in relation to the budgetary protection and stability offered by the Fund”.

- Treasury management of the Fund was effective and current arrangements – with the EIB – should stand (but the EIB should take more risk ‘on its books’ for lending to investment grade countries).
- 9% is an appropriate level for the target rate and should be maintained.
- The provisioning mechanism works well and is appropriate.
- In terms of the adequacy of budgetary resources, payments to the Fund (due to losses) are capped by the smoothing mechanism at EUR 100 million. Both the mechanism and the EUR 100 million limit were deemed to be “appropriate”.
- Payments to the Fund (arising from additional disbursements) were, however, projected to rise – above the current annual budget allocation of EUR 200 million. The review recommended that the annual budget allocation should be increased to EUR 250-300 million if the external lending aspirations of the EIB (and related increase in Budget exposure) are realised.

In terms of governance, although the Commission entrusts financial management of the Guarantee Fund to the EIB, the Commission supervises the mandate, and monitors and reviews the Guarantee Fund mechanism. The Commission is also responsible for regular reporting on the situation of the Fund – and its management – to the Parliament, the Council and the Court of Auditors. The latest report is dated July 2010 and is accompanied – as usual – by a comprehensive ‘Staff Working Document’ giving full details about the Fund, its investment portfolio and performance, liquidity position and risk management operations.

The Fund appears to be managed prudently by the EIB with financial statements being prepared in accordance with International Financial Report Standards (IFRS). The accounts are audited and certified by an independent auditor. All banks with which deposits are placed have a minimum short-term credit rating of P-1 (Moody’s or equivalent). P-1 (Prime-1) rated issuers are defined to have ‘a superior ability to repay short-term debt obligations’. The Fund operates in one currency only (the Euro), investing exclusively in this currency and therefore avoiding exchange rate risk (and any requirement for hedging instruments).

As mentioned earlier, in terms of the EU budget and mitigating any current risks, the external independent evaluation of the Guarantee Fund reported very positively; particularly with regard to the provisioning mechanism and the appropriateness of the target rate. In the Official Journal of the European Union (9.11.2010), the Court of Auditors similarly reported that the Guarantee Fund was managed in a ‘satisfactory manner’, adding that ‘appropriate actions have been taken to monitor the impact of the financial crisis on the Fund’s portfolio’.

However the evaluation report states that ‘over the next 10 years, the repayments to the EU/EIB are forecast to rise from EUR 1.5 billion to nearly EUR 4.5 billion. This represents a significant increase in the level of credit risk to the EU’. By itself, this statement is correct – however, in practice, any increase in associated credit risk is offset by the fact that, in tandem, provisioning against losses is similarly re-sized.

4.3.2. Guarantee of Loans to Member States

In order to ensure that loans granted under these instruments can always be reimbursed within the limits of own resources (described later) even in the worst case scenario of default on all loans due, the total reimbursement of loans guaranteed by the EU budget in any budget year is limited to the margin ('headroom') between the own resources payments ceiling and the Financial Framework payments ceiling. In the following text, this point is illustrated with reference to the 2011 EU Budget.

Table 5: The EU Budget 2011 (EUR billions)

	Payments (EUR billions)	Percentage
Sustainable Growth		
- Competitiveness	11.6	
- Cohesion	41.7	
<i>Sub-total</i>	53.3	42%
Preservation & Management of Natural Resources		
- Direct aid & market-related expenditure	42.8	
- Rural develop. environment & fisheries	13.5	
<i>Sub-Total</i>	56.3	45%
Citizenship, Freedom, Security & Justice		
- Freedom, security, justice	0.8	
- Citizenship	0.6	
<i>Sub-Total</i>	1.4	1%
The EU as a Global Player	7.2	6%
Administration	8.2	6%
Total	126.5	100%
% of EU-27 GNI	1.01%	

Source: <http://eur-lex.europa.eu/budget/data/LBL2011/EN/GenRev.pdf>

Table 5 provides the amounts allocated under different expenditure headings for the 2011 budget. The expenditure authorised by the budget totals EUR 126.5 billion. Accompanying text estimates the gross national income (GNI) of the 27 Member States to be around EUR 12.5 trillion. Thus the budget represents 1.01% of EU-27 GNI.

Money to fund the Budget comes from EU Member States. The individual contributions are summarised in Table 6. In line with shareholdings, the largest contributions come from Germany, France, Italy and the UK.

Table 6: Financing the 2011 EU Budget (EUR millions)

COUNTRY	VAT OWN RESOURCE	GNI OWN RESOURCE	UK CORRECTION	REDUCTION IN GNI FOR NL & SE	TOTAL NATIONAL CONTRIBUTIONS	PERCENT
Germany	1,617.9	19,221.1	182.2	168.7	21,189.9	19.6%
France	2,687.3	15,429.7	823.1	135.4	19,075.5	17.6%
Italy	1,865.2	11,912.3	635.5	104.6	14,517.6	13.4%
UK	2,567.5	13,313.3	-3,079.1	116.8	12,918.5	11.9%
Spain	1,194.1	7,938.4	423.5	69.7	9,625.7	8.9%
Netherlands	297.2	4,548.6	43.1	-625.1	4,263.8	3.9%
Poland	552.5	2,776.5	148.1	24.4	3,501.5	3.2%
Belgium	447.1	2,726.5	145.4	23.9	3,342.9	3.1%
Sweden	153.8	2,642.6	25.0	-141.7	2,679.7	2.5%
Austria	292.6	2,173.0	20.6	19.1	2,505.3	2.3%
Denmark	288.0	1,844.9	98.4	16.2	2,247.5	2.1%
Greece	320.6	1,753.5	93.5	15.4	2,183.0	2.0%
Finland	241.2	1,380.2	73.6	12.1	1,707.1	1.6%
Portugal	245.0	1,231.3	65.7	10.8	1,552.8	1.4%
Czech Republic	198.4	1,054.3	56.2	9.3	1,318.2	1.2%
Ireland	199.4	1,002.3	53.5	8.8	1,264.0	1.2%
Romania	145.3	965.1	51.5	8.5	1,170.4	1.1%
Hungary	130.7	745.8	39.8	6.5	992.8	0.9%
Slovakia	79.8	518.7	27.7	4.6	630.8	0.6%
Slovenia	53.4	268.4	14.3	2.4	338.5	0.3%
Bulgaria	50.0	262.4	14.0	2.3	328.7	0.3%
Luxembourg	43.8	220.2	11.7	1.9	277.6	0.3%
Lithuania	40.9	205.4	11.0	1.8	259.1	0.2%
Cyprus	26.1	131.1	7.0	1.2	165.4	0.2%
Latvia	20.3	129.0	6.9	1.1	157.3	0.1%
Estonia	20.0	103.7	5.5	0.9	130.1	0.1%
Malta	8.7	43.5	2.3	0.4	54.9	0.1%
EU-27	13,786.8	94,541.8	0.0	0.0	108,328.6	100%
Sugar levies					123.4	
Customs duties					16,653.7	
Other revenue					1,421.4	
Total Revenue					126,527.1	

Source: Adapted from http://ec.europa.eu/budget/budget_detail/current_year.en.htm

Notes: There are three main categories of 'own resources': traditional own resources (composed of sugar levies and custom duties), VAT-based resources and GNI-based resources. These are supplemented by various correction mechanisms.

As can be seen, total revenue = total expenditure (EUR 126.5 billion). The operation of the EU is based on the principles of a balanced budget.

As noted earlier, the 2011 Budget represents around 1.01% of EU-27 GNI. However the ceiling for own resources is set higher, at 1.23% for 2011. This is the limit placed on the EU Budget to call own resources payments from Member States. The margin under the own resources ceiling is therefore around 0.22% - and it is this margin ('headroom') that is used to provision for default on a guaranteed payment.

The headroom available during the period 2007-13 for guaranteed reimbursements (margin) is presented in Table 7. It is the difference between the Own Resources Ceiling and the Amounts Budgeted (or Payment Appropriations in future years).

Table 7: Margin Under the Own Resources Ceiling (EUR millions)

	2007	2008	2009	2010	2011	2012	2013
Own Resources Ceiling (%)	1.24%	1.24%	1.24%	1.23%	1.23%	1.23%	1.23%
Own Resources Ceiling (EUR million)	151,356.5	152,445.6	144,015.7	147,188.0	151,954.5	157,948.3	164,262.3
Payment Appropriations in the MFF (EUR million)	122,190.0	129,681.0	120,445.0	134,289.0	134,280.0	141,360.0	143,331.0
Amounts Budgeted (EUR million)	113,845.8	115,771.3	113,410.3	122,955.9	126,527.1	-	-
Margin (EUR million)	37,510.7	36,674.3	30,605.4	24,232.1	25,427.4	16,588.3	20,931.3

Although the exact budgetary calculations involve a number of complications and intricacies, the arithmetical argument appears to make sense. If you multiply 126.5 by (1.23/1.01) it gives just over 150 (the exact figure shown above for 2011 is EUR 151.9 billion).

Thus the amount available (headroom) in 2011 is EUR 25.4 billion. This compares with potential risk exposure ('total to cover') of EUR 5.8 billion (see Table 8) – leaving an additional margin or safety net of EUR 19.6 billion.

Table 8: Liabilities to be Covered by Headroom in the EU Budget (2011)

CONTINGENT LIABILITIES ARISING FROM...	EUR BILLION
Estimated BoP Payments <i>Latvia, Romania & Hungary = EUR 14.6 billion</i>	2.444
Estimated EFSM Payments <i>Irish programme</i>	0.345
Estimated MFA Payments + Estimated Euratom Payment + EIB External Lending Mandate	3.038
Maximum Total to Cover	5.827
Headroom	25.427
Remaining Margin	19.600

To calculate the liabilities summarised in Table 8, the Commission establishes a forecast of all payments becoming due in each year (interest and capital) for all continent liabilities arising from the EFSM, BoP, MFA, Euratom and the EIB's external lending. The 'remaining margin' is calculated by subtracting these payments from the Budget headroom. This figure shows the extent to which additional obligations could be covered. Note that the remaining margin is calculated using the very conservative assumption of defaults on all loans (none of the debtors pay). On top of this, the Guarantee Fund for External Actions provides an additional layer of Budget protection (estimated at around EUR 1.5 billion for 2011).

4.4. Commentary

This chapter has considered the credit risk exposure of the EU budget in relation to guarantees given (and lending operations implemented directly) by the European Union, and indirectly through the EIB external mandates. Through necessity, we have relied on evaluations – conducted by others – of the alternative approaches to loss provisioning: creation and maintenance of a dedicated fund (the Community Guarantee Fund) and a reliance on 'headroom' within the EU Budget.

The two approaches appear to have developed for different yet understandable reasons. Lending and guarantees provided directly by the EU are aimed at operations within the EU. As such, these instruments are essentially provided by EU shareholders for EU shareholders, and provisioning from fiscal headroom in the budget appears reasonable. The EIB guarantee, on the other hand, covers operations outside the EU – for which additional comfort is provided to Member States through a specific provisioning fund. The mechanics of each arrangement appear to be 'fit for purpose' and, *ceteris paribus*, they seem to achieve their objectives. Our research has uncovered no particular defects or flaws. Nor has it suggested that one approach or set of arrangements is better (or worse) than the other. It is the size of the respective provisioning that is probably the more useful focus.

Both approaches have been tested against hostile scenarios – some might suggest unfeasibly hostile conditions (such as 100% loan defaults) – and appear to have survived with minimal if any impact on the EU budget. The material we reviewed on direct lending and guarantees was compiled by the Commission itself whereas that for the Guarantee Fund ('indirect' lending and guarantees) was prepared by consultants. To that extent the latter set of evaluation material benefits from an independent analytical assessment. Detailed loss simulation tests (and their results) are reported in considerable detail, for example. Notwithstanding this, both evaluations conclude with positive findings. To truly comprehend the possible exposure of the EU budget, however, it would be necessary to understand far more about the credit standing of the beneficiaries of the loans and guarantees (under both approaches). This is not a trivial exercise, however, and lies well beyond the scope of work reported here.

The issue of 'fitness for purpose' is not a static concept. It is dynamic in the sense that it needs to be revisited as both the direct and indirect instruments develop in the future, in response to different stimuli and requirements. In this context, our concern is less with facilities extended within the EU-27 (unless the credit quality of Member States deteriorates significantly – most are currently high, or very high, investment grade) and perhaps more with external activity. The provisioning against losses associated with EIB-related external lending clearly needs to be monitored if the Bank is going to ramp-up its development finance operations (in the absence of the Bank undertaking more own-risk lending). Indeed,

future aspirations for the EIB in the development finance arena might need to be tempered by the Budget's ability and willingness to expose itself to greater risk.

One family of entities which appears to have been largely overlooked in much of the literature that we have reviewed is the credit rating agencies. We studied their material – such as rating research documents and surveillance reports – in some detail. After all, the agencies, in particular Standard & Poor's and Moody's – rate both the EU and the EIB (and, for that matter, the EBRD as well). This provides a further level of independent scrutiny focussed specifically on credit characteristics and trends that could be perhaps leveraged to a greater extent in terms of monitoring EU Budget exposure going forward.

Looking ahead, there may be other developments (some foreseeable and others as yet unforeseen) which could place different pressures on the EU Budget. The EIB's evolving external mandate has already been mentioned in this regard. Should the Euro stability instrument mechanism change, for example, perhaps becoming inter-governmental (rather than Budget-based), this could change the picture. And with many pressures on the EU Budget to deliver more – and an enthusiasm for more sophisticated partnership-based financing operations – it is essential that procedures should be in place to automatically evaluate and monitor (and report) any and all budgetary implications – specifically those related to the adequacy of loss provisioning.

In closing, our Terms of Reference specifically asked us to consider the implications of EU Budget guarantees for sovereign debt related to balance of payments support. The short answer is that there are no specific implications. The reimbursement of any borrowing raised by the Commission to finance a balance of payments loan has to be certain. Should a beneficiary country not repay its debt, the Budget would have to provide the funds to pay back all obligations from the related borrowing. If liquid assets are insufficient, the Commission would call on Member States to provide the necessary funds (in exactly the same way that if provisioning funds and/or headroom became exhausted, recourse to Member States would be made).

5. CONCLUSIONS AND RECOMMENDATIONS

This section sets out our conclusions in relation to the implications of EIB and EBRD co-financing for the EU budget with respect to the key issues raised within the terms of reference with reference to budgetary liability and management, governance and accountability, budgetary control, transparency and visibility. It also explores specific issues raised by the external mandate. Where appropriate recommendations are made in light of these conclusions.

Conclusion 1 – That the development of co-financing instruments poses no direct risks to the budget in terms of financial liability.

As we show in the analysis herein there are in fact few, if any, concerns in a formal sense in terms of budgetary liability. All of the co-financed instruments involve allocations to programmes which are capped in size and so none of these instruments pose a risk to the budget beyond that which is initially committed. Even in those cases in which the financial instrument involves a form of guarantee (e.g. the SMEG guarantee fund or the LGTT guarantee fund) there remains no liability beyond that which was originally committed during the design of the instruments. The potential exception to this is the guarantee given to the EIB in terms of the external mandate. We comment on that separately below.

Conclusion 2 – That the Guarantee Fund instrument which underpins the External Mandate of the EIB is an appropriate instrument, which is appropriately provisioned and poses little, if any, risk to the EU budget.

Chapter 4 examines the nature of the External Lending Mandate which underpins EIB operations in non-EU countries given in the form of the guarantee fund. Our findings here are in agreement with earlier evaluations which have been undertaken of the guarantee fund, namely that it is effectively managed, appropriately provisioned, has strong governance mechanisms in place and poses little, if any, risks to the budget. However we acknowledge that this may change if the EIB were to significantly increase its external lending activity, assuming that this were not taken at the Bank's own risk.

Conclusion 3 – That the guarantees covering loans extended to Member States (for the MFA balance of payments facility and the European Financial Stabilisation Mechanism) are adequately provided for through 'headroom' in the EU budget and, as such, pose no particular threat to the EU budget.

Through a worked example, Chapter 4 examined the adequacy of headroom within the EU budget by looking at (a) total guaranteed amounts (liabilities) outstanding, and contrasting that with (b) the difference between the Own Resources Ceiling and the Amount Budgeted (the margin or 'headroom'). We found that the actual headroom exceeded the liabilities by a multiple, providing comfort about the adequacy of this particular loss provisioning arrangement. Indeed, that adequacy appears more than sufficient before account is taken of additional layers of available budget protection (such as the Guarantee Fund itself).

Conclusion 4 – That while the EP maintains formal budgetary control through the decision to develop co-financing instruments it is more difficult to maintain practical control over the way in which the budget is dispersed.

The key issue here, which is discussed extensively in the report, is the extent to which the creation of co-financing instruments makes the EP's job more difficult in terms of exercising budgetary control. Our conclusions are that while the EP, through its Treaty powers, is involved in the framing of these instruments and in the decision to place parts of the budget at the disposal of financial intermediaries, so maintaining levels of control in the formal sense, a number of challenges present themselves in terms of the arms-length nature of that control following the implementation of co-financing. In particular, control is clearly reduced in a framework in which a financial instrument is run via an intermediary (such as the EIF) who then passes management of financial disbursement to a further intermediary (e.g. a bank).

Furthermore, budgetary control is also reduced with the development of co-financing in terms of the relationship between the European Parliament and the implementing institutions. For example, while the Commission is formally accountable to the European Parliament for the implementation of EU policy, the control which the EP can exercise over either the EIB (which is owned by the member states) or the EBRD (which the EU has a very minor role in the governance of) is much more limited.

Recommendation – our key contention is that **further research into what the implications are for budgetary control needs to be undertaken**. Without it, such concerns remain. In the absence of detailed insight into what is happening 'on the ground' it is very difficult to assess how real problems of budgetary control are in actual terms.

Conclusion 5 – That the development of co-financing instruments is broadly compatible with the strategic objectives of the EU

and

Conclusion 6 – That co-financing raises mixed conclusions in terms of the extent to which it leads to effective policy delivery.

The EP is instrumentally involved in the decisions to create these instruments in the first place. There is also clear evidence that co-financing has generally been undertaken in areas which have seen some considerable success in delivering EU policy priorities, such as innovation, research and competitiveness – all of which are fundamental strategic objectives of the EU. Many of these instruments have delivered a number of highly impressive economic outcomes – a particularly notable achievement given the context of the financial and economic crisis.

However, there has been considerable variation in the capacity of the 'new' member states and the SME sectors to benefit from these instruments leading to concerns that, at present, co-financing may be best suited to those markets which are relatively developed. This is particularly demonstrated with the ongoing and severe problems caused by both the financial crisis and the low levels of absorption of the structural funds in many of these states – problems which it is perhaps unrealistic to expect co-financing in isolation to overcome.

Conclusion 7 – That co-financing poses some problems for the EU in terms of transparency but that such problems can be ameliorated with more effective auditing.

There are two particular aspects to the transparency issue. The first is that co-financing, through the use of chains of command and the cascade of responsibilities simply makes it more difficult for the EU institutions themselves to track how the budget is spent and to evaluate the effectiveness of that spending. The second relates to the tensions which exist at the heart of co-financing with the EIB and EBRD, in particular, in terms of the EU's desire for transparency and openness alongside the EIB's and EBRD's desire to respect their commercial confidentiality, which are central to their lending activity. Such tensions are very difficult to ameliorate as they are at the heart of the adoption of co-financing.

Recommendations – We make two suggestions here. First, we would strongly **encourage a robust form of audit by the European Court of Auditors on the basis of an expanded mandate** to review not only the EU contribution to a co-financed instrument but the whole of the contribution including that made by the EIB and/or EBRD. Without this, audit becomes only partially effective. Second, we suggest that a desire for transparency must lead to a very **different type of evaluation** which places a premium on asking difficult questions of instruments which may at first glance seem to have delivered sub-optimal outcomes, rather than continuing with the existing pattern of audit which seems to be focused on EU 'success stories'.

Conclusion 8 – That co-financing poses particularly acute problems for the EU in terms of visibility.

In a context in which visibility of many EU schemes is low, co-financing poses particularly acute problems in terms of visibility, here understood as the extent to which the recipient is aware of the EU's role. Overall, in spite of the fact that there has been a consistent pattern in which the EU has attempted to develop a number of schemes designed to enhance visibility, the existing evaluations of all of these schemes points to a pattern of low stakeholder and beneficiary awareness across the board. At a theoretical level this is hardly surprising – co-financing frequently works through intermediaries who are ultimately responsible for disbursing the funds, so making the EU's role increasingly opaque.

Conclusion 9 – That the consideration of co-financing needs to be undertaken alongside a detailed evaluation of the implications that this may have in terms of the risk appetite within the EIB.

Many of the co-financed instruments contain at their heart mechanisms to insulate the EIB against risk. In providing such instruments, the EU is allocating monies which could potentially be spent elsewhere if the EIB were happy to undertake riskier lending. Yet that comes with a potential cost to both the EIB and the EU as a whole in that the guarantees offered to the EIB effectively act as an insurance policy which allows large volumes of lending at low cost to the beneficiaries. We see this current situation as effectively a trade-off between the costs to the budget in terms of the proliferation of guarantees and the benefits in terms of the protection of the EIB's credit rating and its capacity to lend at low rates. In contrast, the EBRD doesn't enjoy a budgetary guarantee of the sort given to the EIB. This conclusion, then, is intended to further debate as to the appropriate balance which should be taken between promoting a greater risk appetite within the EIB and the provision of EU guarantees.

Conclusion 10 – That any use of co-financing instruments will involve a trade-off between political and financial considerations but that the relative value of such considerations is itself a political judgement.

One of the key questions addressed here is whether there is a trade-off between political and financial considerations in relation to co-financing and how to best evaluate it. We agree that if you sign up to the use of co-financing instruments you implicitly embrace some trade-offs between the benefits of such instruments, which are primarily economic and financial, and the problems, which primarily relate to issues of governance, transparency and visibility. This report provides material for deliberation on this question; we remain of the view that the decision reached will be a matter of political judgement.

6. DISCUSSION

This final chapter considers issues raised during our research which, although related to our study, were not identified as key questions to be addressed in our Terms of Reference. The topics listed below were identified from our reviews of Commission and Bank reports, and from our interviews with Commission and Bank staff. Each is considered in turn in the paragraphs that follow:

- The future for co-financing: overview;
- Standardisation and harmonisation of the new financial instruments;
- The tension between grant intensity and appropriate project support;
- The banks' response to the global financial crisis;
- Ongoing project monitoring;
- Using the EIB and EBRD to maximum effect.

6.1. The Future for Co-Financing: Overview

There was a general agreement amongst all of our interviewees (from each institution) that there will be pressures – and there is an appetite – for more innovative financing as we move from this Financial Perspective to the next. In part, this reflects a philosophical shift at the Commission from a traditional reliance on grants (or buying services) to loan/grant blending, more of these joint instruments and more partnership arrangements. Particularly in the context of possible EU budget constraints, there is a clear desire to do 'more with less' – and engaging budgetary resources with those from the IFIs was identified as a key way of achieving this objective.

It was felt that joint instruments had generally enjoyed a positive track record to date for all of the reasons listed in Chapter 3 – of which complementarity, risk sharing, the instilling of discipline and control, and leverage effects were the most frequently cited. Pure grants – by themselves – were regarded as a 'one-shot game' and a number of interviewees questioned their effectiveness in certain circumstances.

However this has to be put in context. At present, estimates suggest that around 3% of Structural Funds (approximately 1% or less of the total EU budget) is directed to innovative financial instruments. This is very small indeed, however – as mentioned above – it looks set to grow. This raises a number of challenges including the need to ensure policy alignment (with partnering institutions) and the promotion of EU visibility. Blending is clearly not a panacea for every pressure on the EU budget. For some purposes it is neither appropriate nor desirable. Several interviewees mentioned that care needed to be taken in some situations to ensure that blended products do not become overly-sophisticated or undermine/undercut legitimate private sector activities. Notwithstanding, the future trend seems clear. The ongoing challenge for the Commission then becomes how to shape combined Commission and Bank resources and expertise in the future to best further EU policy objectives.

6.2. Standardisation and Harmonisation of the New Financial Instruments

Building on comments made above and with an eye on the future, without prompting a number of our interviewees turned to the issue of instrument standardisation. Described as a 'panoply of instruments', interviewee concerns with current initiatives focussed on a lack of consistency, coherence and understanding. Interviewees reported that a number of Member States, regions and MEPs themselves found the different procedures, rules and (sometimes overlapping) eligibility criteria associated with different instruments difficult to comprehend. Four or five different sources of funds available for energy efficiency initiatives were cited as but one example. On top of this, interviewees were aware of some current interest in extending the range of financial instruments even further (some DGs were reported to be interested in replicating RSFF-type arrangements, for example).

Strong cases were made for simplifying and streamlining the current arrangements, and a need to send 'joined up' messages particularly to potential beneficiaries. 'Efficient', 'not political' and 'not over-engineered' were frequent comments made to us. Instead there were calls for simple instruments that would be easy to replicate and could be deployed quickly, more concrete parameters for blending and the need for a coherent framework for the consolidation of existing initiatives and development of new ones. To be fair, we are aware of work that the Commission is currently progressing which appears to go some way in terms of addressing these specific concerns.

Having listened to various arguments, we are drawn to the concept of and desire for standardisation. Our own list of the instruments currently available (appended to this report) stretches to over 30 pages. Looking back, there may have been a justification for 'learning by doing' in the past. But given earlier comments about the potential future growth of blended products, it would appear sensible to carry the lessons learned forward on a consolidated basis through a more standardised approach. There is clearly no one-size-fits-all solution and standardisation objectives need to remain realistic – and probably fairly high-level; perhaps focussing on the fundamentals (common rules) yet still allowing for minor adaptations to be made to reflect different realities in different circumstances.

6.3. The Tension between Grant Intensity and Appropriate Project Support

During our interviews, a number of concerns were raised about pressures within the Commission to distribute grants to the fullest extent possible. With Cohesion Funds, for example (EUR 308 billion for 2007 - 13), grants can be used to cover up to 85% of project costs. This was reported to be sometimes viewed as a target; not as a ceiling.

Interviewees drew distinctions between sectors, pointing to the fact that 85% grant funding might be appropriate in some sectors (waste water was mentioned) but not in others. It was suggested that in the transport and renewables sectors, for example, current levels of grant intensity were simply too high and, critically, this was impacting negatively on projects and project development. It was reported that high levels of grant intensity worked against some initiatives designed to enhance the involvement of the private sector and efforts to establish effective public-private partnerships in some regions. One interviewee commented, 'If you want to dump Cohesion Funds into a country, instead you should be supporting PPPs'.

The use of grant funds seems entirely legitimate in direct response to market weaknesses or failures – however this needs to be carefully assessed. In situations which provide a return on investment (revenue generating projects, for example), there is less need for grants. Transactions should be structured around cash generation with grants being used to cover the funding gap alone. Over-provision of subsidy sends adverse signals to project counterparties and erodes the incentives on them to perform. It reduces the pressure to explore alternative financial structures and the possible use of commercial funding (which, otherwise, might have been more appropriate). As another interviewee put it, ‘the priority should not be getting rid of money quickly’.

6.4. The Banks’ Response to the Global Financial Crisis

In response to the global financial crisis, both the EIB and the EBRD have demonstrated their flexibility and the fact that, if required, they can ramp-up operations significantly and very quickly. These operations have been directed to specific projects or, more generally, to capacity building (complementary to project-related activities).

This point was made earlier in our report but we felt it worth repeating here. It underscores the fact that both banks represent important instruments of policy delivery for the EU – in a further way that has not received much attention in the literature to date.

6.5. Ongoing Project Monitoring

The adequacy of project monitoring is a subject that was raised in a number of the reports that we reviewed. It has also been highlighted previously by NGOs (in the context of disclosure, transparency and visibility) and was mentioned by our interviewees – particularly those from the Commission. It was suggested that the EIB, although good in terms of publicising new project activity, still provided poor monitoring and follow-up on the progress of on-going projects supported under the external mandate.

This would appear to be an issue that still needs to be addressed. Loan/grant blending introduces specific challenges in terms of disclosure and transparency. Attention needs to be focused on ensuring that appropriate monitoring procedures are in place to support the roll-out of more blended products in the future.

6.6. Using the EIB and EBRD to Maximum Effect

A number of reports that we have reviewed and some of our interviewees called on the EIB to undertake more development finance-related activity, with a clear message that ‘own risk’ operations should be extended (for external lending) and less reliance should be placed on the EU guarantee. This might be a long-term objective – and, in that context, it would possibly have our support. However we would be cautious to suggest that much could or should be achieved in the short term with the bank structured and functioning as it currently does. The bank’s ‘AAA’ credit rating lies at the heart of its business model and a major shift in risk appetite, all other things being equal, could endanger that rating.

The EIB started operations as a wholesale bank – part of the Treasury ‘play’; a conservative public sector lender lending to sovereign and public sector entities. It then evolved to lending against sovereign or bank guarantees – or to projects with (then) monoline-provided

credit enhancement insurance. Next came guarantees with post-construction releases; once projects had transitioned into steady-state operations and certain other conditions had been met. Today, in particular circumstances, the bank is prepared to go on-risk from the outset of a project; through construction and into operations.

This transition in terms of risk appetite has happened gradually, although the pace of evolution does appear to have hastened recently with the bank accepting more commercial risk today. However in most of its operations the EIB remains a very conservative lender. In the past, project risk and credit risk were effectively decoupled. Risk assessment was largely about ticking boxes for economic appraisal. Now there are real project risks to assess and a number of interviewees questioned the EIB's capabilities in that regard. And with an EU guarantee standing behind most of its external lending operations, it is difficult to imagine that there has been much pressure on the EIB to develop its credit analysis capabilities and overall credit culture. This is in stark contrast to the EBRD which benefits from no such guarantee. EBRD operations place no contingent liability risks on the EU budget at all – which might make the bank and its operations more attractive to the EU in the future. The EBRD does take risk and, as a result, has developed a strong credit culture over the last two decades. The creditworthiness of its operations is a primary concern.

There are other characteristics that draw distinctions between the two banks. The EBRD lends commercially at market rates. Its attractiveness to borrowers flows directly from the value added it provides. In contrast, the EIB sets the margin on its on-lending on a cost-recovery basis. For this reason alone, price comparisons – in isolation – between the two institutions become meaningless.

The lending volumes achieved by the EIB (discussed in Chapter 2) are undoubtedly impressive however this has very much been the focus for the bank. Interviewees pointed to the fact that the EIB had particular strengths when lending to large infrastructure projects, for example. Interviewees at the EBRD, on the other hand, were able to point to success with smaller to medium-sized operations often in secondary cities or municipalities – with more focus on a strong local presence, and support with structuring, tendering and procurement, and project implementation. But the EBRD does not just lend small. It has developed recognised experience in particular asset classes, for example sustainable energy and renewables, energy efficiency and the water sectors. And its focus on transition impacts and market economics is reflected in its sector reform capabilities and associated conditionality which finds expression in lending agreements. As an aside, calls for greater conditionality to be incorporated in lending documents generally were made by a number of our interviewees.

More own-risk lending at the EIB would require institutional capacity building; particularly focussed on credit risk analysis. More development finance activity would require the bank to work in different ways – with a strong, local (perhaps permanent) presence in more countries/regions. Before considering these developments, however, it would be prudent of the Commission to take stock of what already exists. There would appear to be little point in the EIB simply replicating what other development finance institutions already do and provide. We later return to this central issue of understanding and using the strengths of each bank to the EU's benefit.

Although not a popular line of argument, a couple of our interviewees tried to 'position' the EIB and the EBRD in different ways and draw a clear line of separation between them. Examples included the following:

- The EIB could undertake large projects whereas EBRD would focus on smaller operations.
- The EIB could focus on lending to the public sector whereas EBRD would concentrate on private sector activities.
- The EIB could focus on some jurisdictions whereas EBRD would operate elsewhere.
- The EIB could lend to certain sectors; the EBRD lending to others.
- The EIB could concentrate on lending at a sovereign level, whereas the EBRD could focus on sub-sovereign operations.

We warmed to none of these arguments and, indeed, would specifically counsel against trying to draw overly-simplistic distinctions between the two financing institutions. In truth, the banks share a number of similarities which make them both strong candidates for partnering with the EU.

However, in terms of partnering, the strength of the banks lies not in these similarities, but in their differences. The EU needs to ensure that it understands these differences well – particular those that relate to the EBRD. One take-away from a number of our interviews was that, although people were familiar with the EIB, rather less was known in detail about the EBRD; its characteristics, capacity and capabilities. Through having a good understanding of both banks, the EU can use them to its advantage in order to carry the most appropriate partnership arrangements forward effectively and efficiently into the next Financial Perspective.

ANNEX 1 EIB AND EBRD CO-FINANCING INVENTORY

Financing from the EU contributes to a number of joint initiatives with the EIB and the EBRD (and others) from different headings under the EU budget – as well as from the European Development Fund – in a number of different ways. These contributions are summarised below under the following headings:

Within the EU:

- RSFF (EIB)
- CIP (EIB)
- LGTT (EIB)
- JASPERS (EIB & EBRD)
- JESSICA (EIB)
- JEREMIE (EIB)
- JASMINE (EIB)
- ELENA (EIB)
- Marguerite (EIB)

Outside the EU:

- The EU-Africa Infrastructure Trust Fund (EIB)
- The ACP-EU Energy and Water Facilities Pooling Mechanism (EIB)
- The Neighbourhood Investment Facility (EIB & EBRD)
- The Investment Facility for Central Asia (IFCA)
- The Western Balkans Investment Framework (EIB & EBRD)
- The Facility for Euro-Mediterranean Investment and Partnership (EIB)
- The External Mandate (EIB)
- The ACP Mandate (EIB)
- The Northern Environmental Partnership
- EBRD-Managed Nuclear Safety Funds
- The Eastern Europe Energy Efficiency and Environment Partnership (E5P)
- Other Initiatives (EIB & EBRD)

Initiatives within the EU

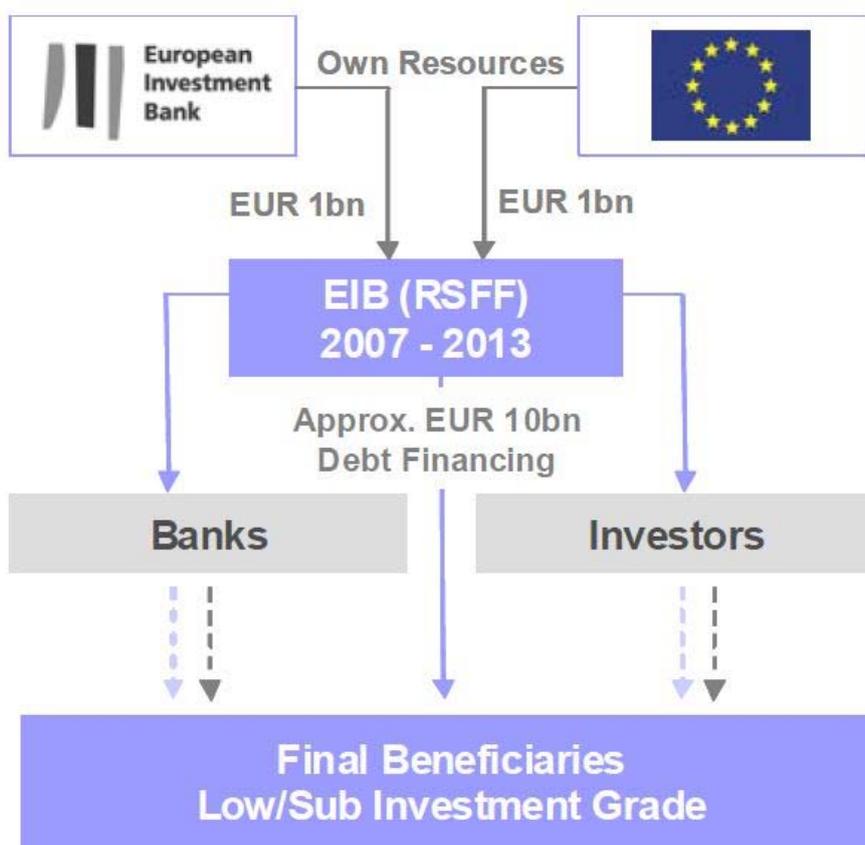
1.1 The Risk Sharing Finance Facility (RSFF)

In 2007 the Commission and the EIB jointly established a risk-sharing finance facility to support and accelerate research and innovation across Europe (EIB, 2010b). The facility, part of the EU's 7th Research Framework Programme (FP7) and the EIB's programme for Research and Innovation, was designed to partially cover the risks assumed by the Bank when financing higher-risk, yet creditworthy, research-intensive companies and projects. The objective was to improve low and sub-investment grade borrowers' access to debt finance. The RSFF covers the risk born by the Bank – when lending directly to promoters or when guaranteeing loans made by financial intermediaries – through capital allocations and provisions.

The RSFF effectively increases the EIB's capacity for financing more and riskier operations. In this sense, the total loan amount that can be made available is a multiple of the extra provisioning that is set aside (the leverage effect).

The RSFF Co-operation Agreement for the period 2007-13 stipulated that the EC could provide up to EUR 1 billion to the EIB for the facility – matched by another EUR 1 billion from the EIB itself (see Figure 6). That is EUR 2 billion risk coverage for potential losses (non-repayment of RSFF loans by borrowers/beneficiaries).

Figure 6: Overview of the Risk-Sharing Finance Facility (RSFF)



Source: Evaluation of Facilities under the RSFF, EIB

At the end of 2009, EUR 433 million was transferred from the Commission (EIB, 2010a). Out of that EUR 433 million, 90% (EUR 390 million) had been committed. This was matched by EUR 772 million from the EIB. A total of 137 RSFF project were being supported. The facility was estimated to trigger a total EUR 16 billion of investments in research (*op cit*), giving an estimated leverage exceeding 16x.

1.2 CIP Financial Instruments (GIF & SMEG)

The Commission's Competitiveness and Innovation Framework Programme (CIP) targets small and medium-sized enterprises (SMEs) through business support services and enhanced access to finance. Almost one-third of the CIP budget (over EUR 1.1 billion for 2007-2013) is allocated to financial instruments that facilitate SME's access to finance (EIF, undated). These instruments are not directly available to SMEs, however. Instead, they are implemented by the European Investment Fund (EIF) and selected financial institutions through venture capital funds and loan guarantees. The EIF manages the programme on behalf of the Commission on a trust basis.

The CIP offers two different instruments to SMEs, depending on their stage of development and financing needs (see Figure 7). A High Growth and Innovative SME Facility (GIF) provides risk capital for early-stage – seed and start-up – investments (GIF1) and for SMEs in an expansion phase (GIF2). An SME Guarantee Facility (SMEG) provides guarantees to encourage financial institutions to make more direct finance available to SMEs by reducing their exposure to risk.

Figure 7: CIP Financial Instruments

High Growth and Innovative SME Facility (GIF1 & GIF2)	SME Guarantee Facility (SMEG)
GIF1: early stage (seed and start-up) investments GIF2: expansion stage	Loan guarantees Microcredit Equity and quasi-equity guarantees Securitisation
€ 550 m	€ 506 m

Source: CIP Financial Instruments, EIF

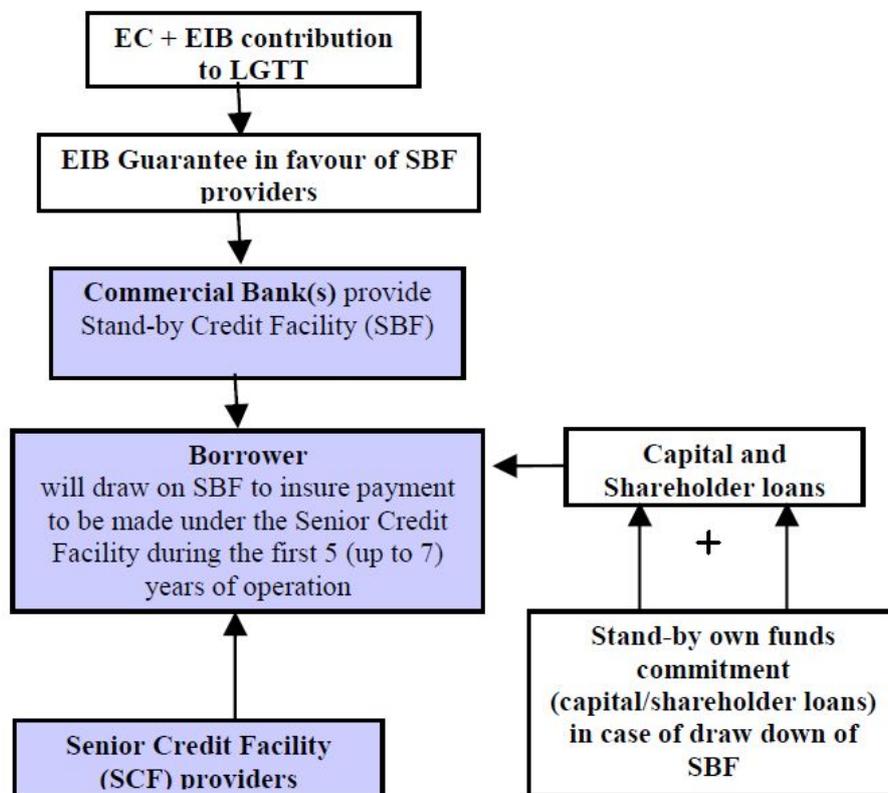
The CIP will come to an end in 2013 and the Commission is currently considering actions and priorities to continue to support the competitiveness of European businesses after that date.

1.3 Loan Guarantee Instrument for Trans-European Transport Network Projects (LGTT)

Early in 2008 the Commission and the EIB signed a co-operation agreement establishing a EUR 5 billion Loan Guarantee Instrument for trans-European transport network projects (LGTT). The LGTT is an EIB guarantee for subordinated debt (in the form of a standby liquidity facility) provided by commercial banks (see Figure 8) (EIB, 2008a). The objective is to provide additional security (contingent mezzanine debt – thereby protecting senior debt) for eligible transport projects; specifically covering traffic (ie. revenue) risk in the first 5-7 years of project operations. This joint risk-sharing initiative is specifically designed to

accelerate private investment in large European infrastructure projects by reducing ‘ramp-up’ risk and, hence, improving financial viability and credit quality.

Figure 8: Loan Guarantee Instrument for TENs Transport (LGTT)



Source: LGTT Factsheet, EIB

Credit enhancements, *ceteris paribus*, place downward pressure on the risk margins applied to senior debt – reducing project costs. The instrument adds value when the cost of the guarantee, to the borrower, is less than the savings that result.

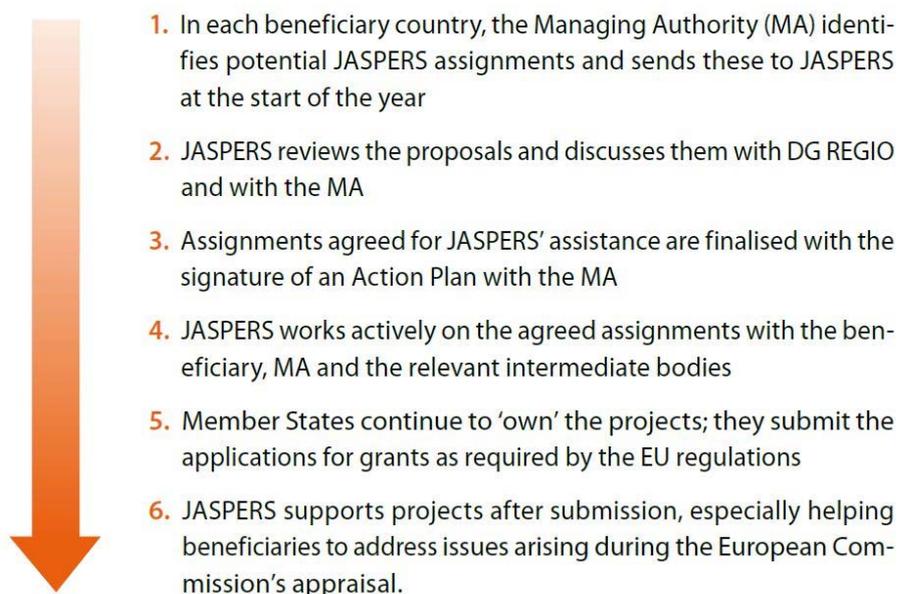
LGTT is financed with a capital contribution of EUR 1 billion (EUR 500 million each from the Commission and the Bank). The capital commitments enable LGTT guarantees of EUR 5 billion to be issued (based on a 20% provisioning ratio). Residual risk is borne by the EIB’s balance sheet. There is no residual risk exposure for the EU budget. To date, four projects have been signed (two road projects in Portugal, one in Spain and one in Germany) and a further 17 are reported to be in the ‘pipeline’. Commission estimates suggest the leverage effect of this instrument could be around 10x.

1.4 Joint Assistance to Support Projects in European Regions (JASPERS)

The co-financed JASPERS initiative – managed by the EIB – focuses on technical support. It is a partnership between the Commission, the EIB, the European Bank for Reconstruction and Development (EBRD) and the German government-owned development bank Kreditanstalt für Wiederaufbau (KfW). It is designed to support the successful implementation of cohesion policy by providing targeted specialist expertise to assist with project preparation in the 12 new Member States, that joined between 2004 and 2007– see Figure 9.

Historically, the quality of project preparations in some jurisdictions had been problematic. The principal aim of JASPERS is to increase both the quality and quantity of projects to be sent for Commission approval. The technical assistance, which is provided free of charge, is thus geared towards accelerating the absorption of available EU Structural and Cohesion Funds. The four JASPERS partners have considerable experience in preparing and financing successful projects particularly in Central and Eastern Europe.

Figure 9: JASPERS – How it Works



Source: JASPERS Brochure 2010, EIB

At the end of 2009, JASPERS had a complement of 67 professional and 10 support staff; located in its Luxembourg headquarters and in regional offices in Warsaw, Vienna and Bucharest (CEC *et al*, 2010a). JASPERS is funded by the Commission and by contributions from the EIB, EBRD and KfW in the form of professional staff time. The published financial statements for JASPERS for 2009 suggest an annual cost of operations for the initiative of around EUR 24 million (CEC *et al*, 2010b).

Contribution to this initiative from the EU is EUR 26 million (in 2010, for technical assistance). Contributions from others are EUR 5.4 million (EIB), EUR 0.5 million (EBRD) and EUR 0.7 million (KfW).

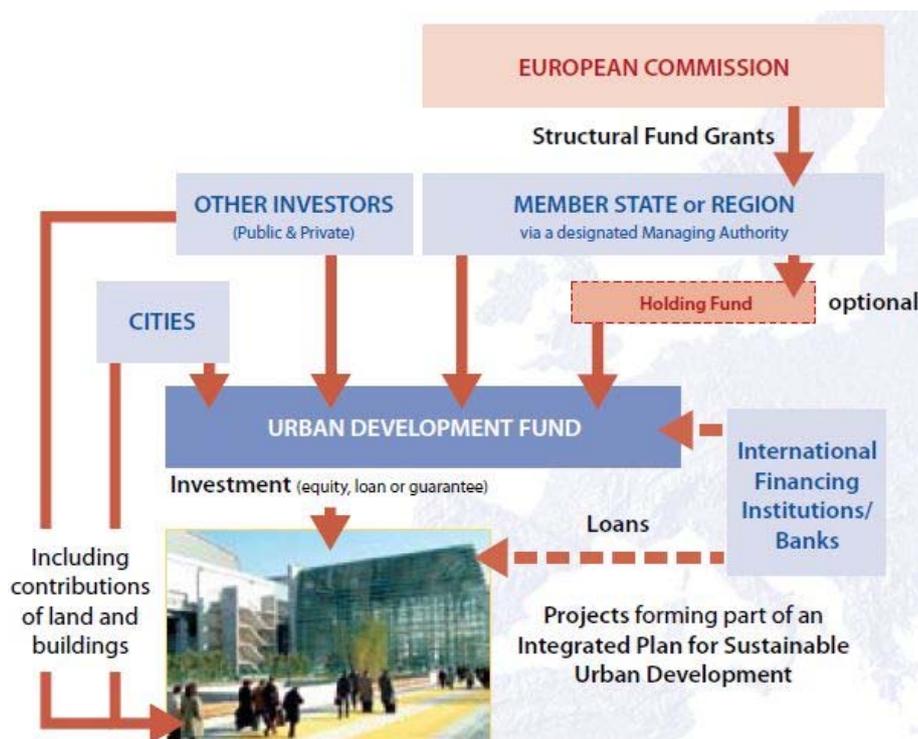
1.5 Joint European Support for Sustainable Investment in City Areas (JESSICA)

JESSICA was launched in 2006 to focus attention on the need for regeneration and renewal in certain European urban areas (CEC, 2006a). It is a joint policy initiative between the Commission, the EIB and the Council of Europe Development Bank – and it is open to participation from other IFIs and FIs. Under JESSICA, Member States and 'Managing Authorities' (authorities responsible for managing assistance from EU Structural Funds) can transform grants from Operational Programmes into repayable and recyclable assistance – equity, guarantees and subordinated loans – to public private partnerships (PPPs) and other projects for urban renewal and development.

Essentially Managing Authorities can use some of their Structural Fund allocations – those supported by the European Regional Development Fund (ERDF) and the European Social Fund (ESF) – to invest in Urban Development Funds (UDFs) to accelerate investment in urban areas (see Figure 10).

The underlying principle is to use ERDF to invest in projects with the expectation of a return on the investment, rather than following the traditional grant approach (that allocated ERDF funding with no expectation of repayment) (EIB, 2008a).

Figure 10: The JESSICA Joint Policy Initiative



Source: EIB website

UDFs represent a market-driven approach as they are expected to at least recover their investment. They must invest in projects within well-defined integrated urban renewal and development plans. Managing Authorities can invest directly in UDFs or – given the challenges associated with managing non-grant instruments – channel their funds to UDFs using holding funds; with the option of employing the EIB as the holding fund manager.

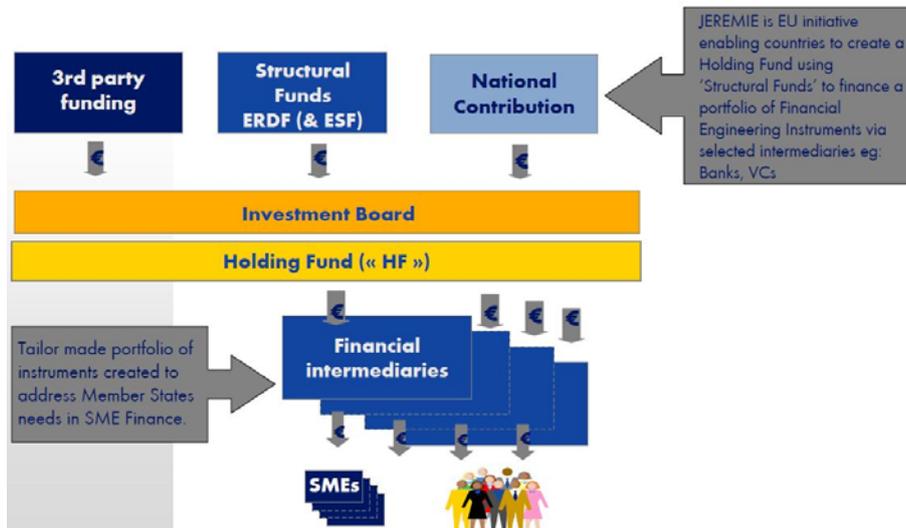
By October 2010, EUR 1.65 billion of Structural Funds had been committed to 19 JESSICA instruments (holding funds and UDFs) in 11 Member States. In 15 cases, the EIB had been mandated to act as the JESSICA Holding Fund – representing EUR 1.5 billion of resources (CEC, 2010c).

1.6 Joint European Resources for Micro to Medium to Medium Enterprises (JEREMIE)

JEREMIE is an initiative of the Commission, the EIB and the EIF. Its primary objective is not dissimilar to the CIP (described earlier) – improving access to finance for the development of micro, small and medium-sized enterprises (SMEs) across the EU – and it works in a similar fashion to JESSICA (through holding funds).

JEREMIE enables Member States (and regions) to invest some of their EU Structural Fund allocations in revolving funds and so recycle financial resources in order to accelerate and enhance investments in enterprises (see Figure 11).

Figure 11: The JEREMIE Concept



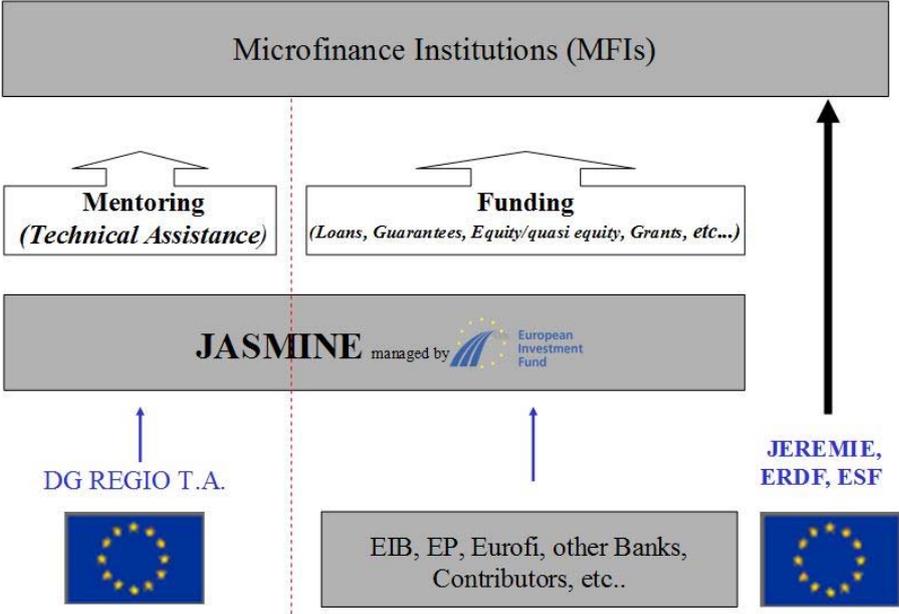
Source: Workshop 2 on JEREMIE Implementation, Brussels, 23rd October 2009

By October 2010, 30 holding funds had been established in 15 Member States. EUR 3.5 billion is committed to these funds, with the EIF acting as the holding fund for 11 JEREMIE operations. Resources primarily consist of an ERDF (or ESF) component matched to a national contribution. Where the EIF is selected as the holding fund, the EIB could refinance through loans the national component of the programme grants. Resources returned to the holding fund from investments undertaken by it, from the reimbursements of loans or left over after all guarantees have been honoured, shall be reused by the Member States specifically for the benefit of SMEs (CEC, 2006b).

1.7 Joint Action to Support Micro Finance Institutions in Europe (JASMINE)

This joint co-financing initiative between the Commission, the EIB and the EIF was launched in September 2008. It is a three-year pilot project (2009-11) designed to provide support and funding to non-bank micro-credit providers and micro-finance institutions in the EU (CEC-DGREGIO, 2010). Its objectives are to promote best practice in the field and to help the providers/institutions to develop (capacity building) and become sustainable. JASMINE combines technical assistance with funding, as illustrated in Figure 12.

Figure 12: The JASMINE Initiative for the Development of Micro-Credit

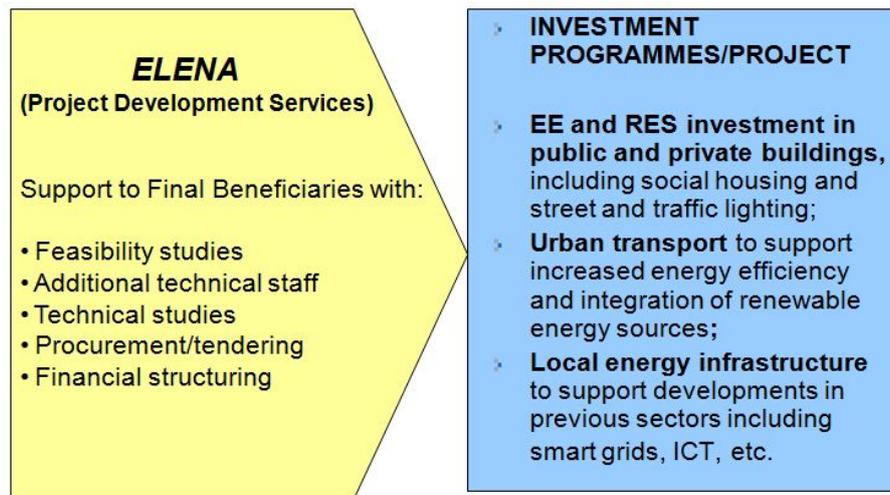


Source: Supporting Micro-Credit Providers with JASMINE, European Union 2010

Technical assistance – in the guise of mentoring, training, information, toolkits and so forth – is delivered by a specialised rating agency and is aimed at capacity building, strengthening governance and management, improving quality and enhancing business reliability. Funding, now available under the EIF-managed European Microfinance Facility, is provided on behalf of the Commission to banks and non-banks to increase the loan offer by the EIF: guarantees (EUR 25 million) and equity/loans (up to EUR 225 million).

1.8 European Local Energy Assistance (ELENA)

The ELENA facility was launched by the Commission and the EIB in late 2009. This joint initiative provides financial and technical assistance to help EU cities and regions implement investment projects in the areas of energy efficiency, renewable energy and sustainable urban transport (EIB, 2010c). The EU contribution covers up to 90% of the costs associated with technical assistance for preparing eligible investment programmes, which the EIB could co-finance. A target leverage factor exceeding 25 has been set (the ratio of investment programme size to technical assistance costs). The ELENA initiative is summarised in Figure 13:

Figure 13: ELENA – Overview

Source: EIB Presentation at the IEE InfoDay, Brussels, February 2009
 EE = Energy Efficiency; RES = Renewable Energy Sources; ICT = Information & Communication Technology

ELENA is a relatively new initiative. The first authority to receive ELENA support was the Province of Barcelona in May 2010 (EUR 2 million grant to finance the technical assistance to develop a EUR 500 million investment programme). The investment programme is focussed on 87.5MWp of photovoltaic installed capacity to realise future energy savings, a significant reduction in CO₂ emissions and job creation (CEC-DGENV, 2010).

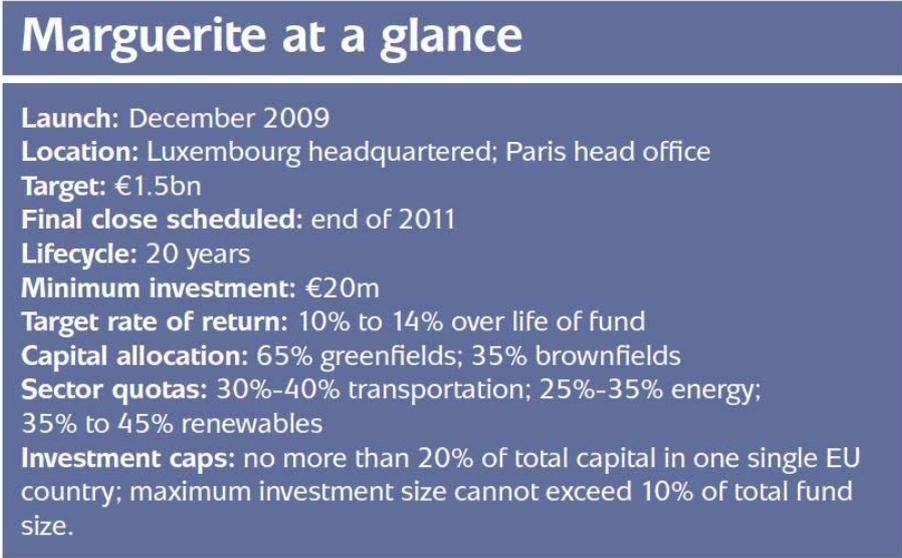
1.9 The Marguerite Fund

Launched at the end of 2009 with initial capital of EUR 600 million, the Marguerite Fund is a pan-European equity fund for infrastructure investments in key EU policy areas (climate change, energy security and trans-European networks) (EIB, 2009). The core sponsors, each with commitments of EUR 100 million, are:

- The EIB
- Caisse des Dépôts et Consignations (CDC)
- Cassa Depositi e Prestiti
- Kreditanstalt für Wiederaufbau (KfW)
- Instituto de Crédito Oficial (ICO)
- PKO Bank Polski

The target equity base of the Fund is EUR 1.5 billion with final closing scheduled for later this year. Key fund characteristics are summarised in Figure 14.

Figure 14: Key Characteristics of the Marguerite Fund



Source: Infrastructure Investor Article (July/August 2010)

The Fund hopes to serve as a model for the establishment of similar funds in the EU wishing to combine a market-based principle of return to investors with the pursuit of public policy objectives. As well as the public sector institutions listed above (the core sponsors), the Fund is open to long-term private sector investors – and discussions are reported to be currently underway with the Commission about making an EUR 80 million equity contribution.

Initiatives outside the EU

Joint initiatives – including co-financing activities – outside the EU are summarised in the following paragraphs under these headings:

- The EU-Africa Infrastructure Trust Fund
- The ACP-EU Energy and Water Facilities Pooling Mechanism
- The Neighbourhood Investment Facility
- The Investment Facility for Central Asia
- The Western Balkans Investment Framework
- The Facility for Euro-Mediterranean Investment and Partnership
- The External Mandate
- The ACP Mandate
- The Northern Environmental Partnership
- EBRD-Managed Nuclear Safety Funds
- The Eastern Europe Energy Efficiency and Environment Partnership
- Other Initiatives (EIB & EBRD)

2.1 The EU-Africa Infrastructure Trust Fund

This EUR 373 million EIB-managed trust fund blends grants from the EU and EU donors with long-term loan finance to support projects designed to bridge Africa's infrastructure deficit; primarily in the transport, communications, water and energy sectors (EIB, 2010d). In terms of grants, the Fund provides four types of support:

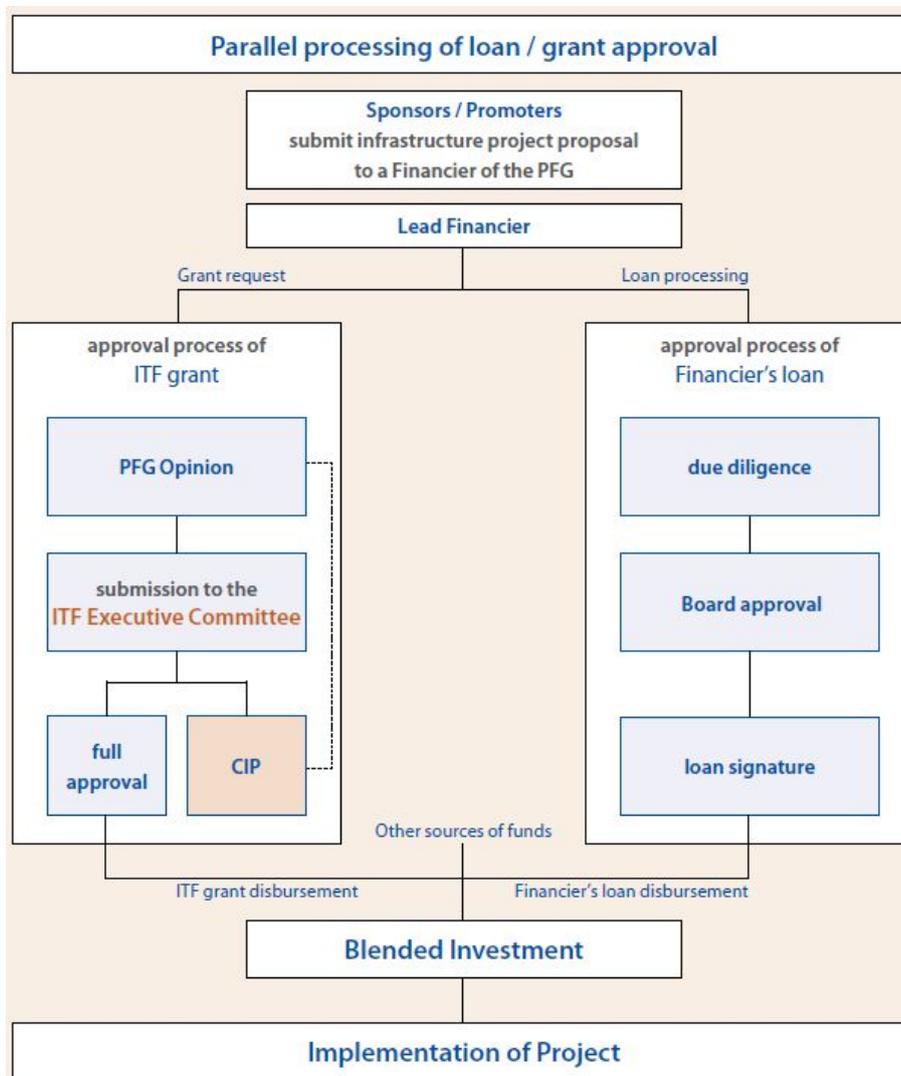
- Interest rate subsidies
- Technical assistance
- One-off grants
- Insurance premia to cover county risk (during the inception phase of the project)

The blending of grants and loans enables promoters and financiers to consider investments which otherwise would not be made because of costly preparatory work, limitations on new borrowing by heavily-indebted, poor countries (HIPC's) or financial returns which do not match the economic benefits of particular projects.

The Fund fosters co-financing and technical co-operation between the Commission (and Member States), the African Union (and Member States), the EIB and participating European

development finance institutions and the African Development Bank. In terms of the mechanics of loan-grant blending (LGB), the parallel project evaluation processes are outlined in Figure 15.

Figure 15: EU-Africa Trust Fund Project Evaluation Process



Source: EU-Africa Infrastructure Trust Fund Annual Report 2009
 PFG = Project Financiers Group; ITF = Infrastructure Trust Fund; CIP = Clearance in Principle

13 new grant operations were approved in 2009, bringing the total number of ITF operations to 21. These operations attracted EUR 120 million in grant funds and were expected to generate investments totalling EUR 1.4 billion (leverage⁴, or a 'multiplier', of over 11 times).

⁴ Leverage can be both financial and non-financial. Non-financial leverage refers to how LGB mechanisms can unblock, accelerate or promote institutional change facilitating more, better and faster investment projects. Financial leverage is the process whereby an original amount of grant can catalyse or mobilise non-grant investment in a project. ITF Trust Fund Annual Report 2009.

In 2010, the Commission announced an additional contribution of EUR 200 million to the ITF, taking its support to over EUR 300 million. Member States contribute a further EUR 84 million.

2.2 The ACP-EU Energy and Water Facilities Pooling Mechanism

This blended grants/loans 'pooling mechanism' aims to co-ordinate EU resources and enhance EU visibility. It targets medium-sized energy and water projects, making them bankable. EUR 40 million is available under the mechanism for each of the two sectors. The key characteristics of the mechanism are summarised in Figure 16.

Figure 16: ACP-EU Energy & Water Facilities Pooling Mechanism

Instruments	Grants (for direct investment), technical assistance and interest rate subsidies.
Eligible Projects: Infrastructure	Medium-sized investment projects that would not be bankable without grant support. The principle objective is to increase access to modern, affordable and sustainable energy or water services in ACP peri-urban areas, growth centres and rural areas.
Eligible Projects: Technical Assistance	Capacity-building actions (when directly linked to a specific investment) and advanced project preparatory studies for candidate projects where energy/water demand, technical feasibility and costs have already been assessed.
Eligible Applicants	EIB, Member State national public bodies or entities governed by private law with a public service mission (such as official development co-operation agencies or ministries in charge of development aid) and the EDFIs.
Project Size	Typically EUR 10 million-EUR 50 million
Level of Grant Support	Investment: EUR 1 million-EUR 5 million (average 10-15% of project; max = 25%)
	Advanced preparatory studies: EUR 1 million

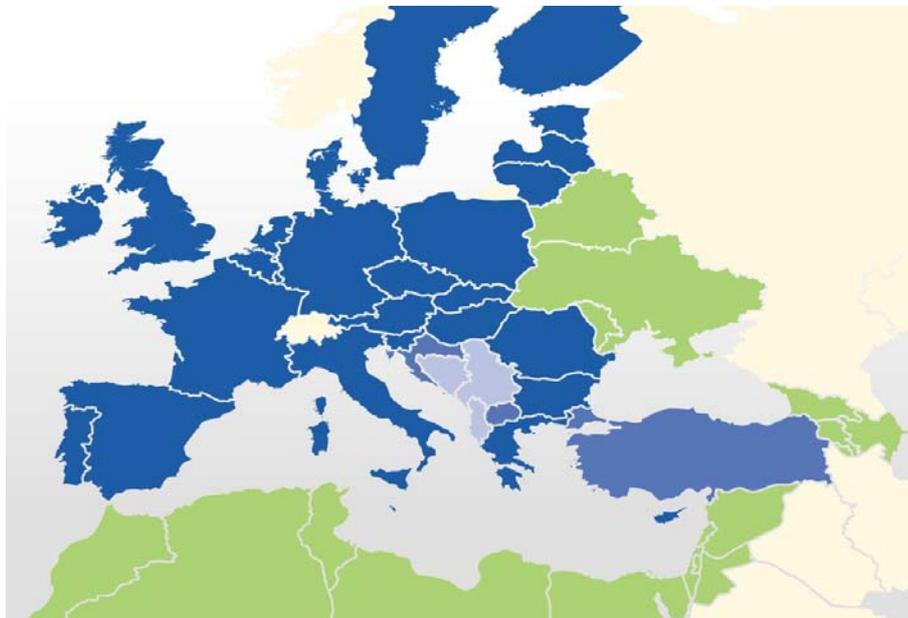
EDFIs = European Development Finance Institutions, a group of 15 bilateral institutions providing long-term finance for private sector enterprises in developing and reforming economies.

The second EU-ACP Energy and Water Facilities were launched in November 2009 and February 2010 respectively. The pooling mechanism became operational under the Energy Facility in October 2010 and is expected to become operational under the Water Facility in March 2011. In the case of the Energy Facility Pooling Mechanism (which is already operational) the first Concept Notes have been submitted for consideration. This will be followed by detailed proposals to be reviewed by an evaluation committee. Therefore, at present (February 2010), there are no grants attributed yet from the EUR 40 million envelope.

2.3 The Neighbourhood Investment Facility (NIF)

The Neighbourhood Investment Facility was established in 2006 by the Commission with the aim of matching long term loans from eligible finance institutions with EU and Member States' grants, from two sources: the EU budget and from an NIF Trust Fund which pools grant contributions from EU Member States. As such, it is another example of the EU leveraging its external assistance, and promoting donor co-operation and joint European operations through partnerships. 'Eligible' finance institutions include the EIB, the EBRD and other multi-lateral and national development finance institutions.⁵ The 'Neighbourhood' refers to 16 of the EU's closest neighbours: Algeria, Armenia, Azerbaijan, Belarus, Egypt, Georgia, Israel, Jordan, Lebanon, Libya, Moldova, Morocco, the Occupied Palestinian Territory, Syria, Tunisia and Ukraine (see Figure 17).

Figure 17: The EU 'Neighbourhood' (countries shown in green)



Source: http://ec.europa.eu/world/enp/index_en.htm

The Facility offers grant funds for capital expenditure (investment co-financing), technical assistance, guarantees, insurance premia and risk capital operations – and focuses on infrastructure investment (transport, energy, the environment and social infrastructure) and private-sector investment (particularly SMEs). The implementation of projects in the NIF is delegated to the lead finance institution (usually the finance institution that submits the project either alone or on behalf of themselves and one or more other finance institutions), for which implementation procedures have been positively assessed. The Lead Finance Institution has delegated monitoring and follow-up responsibilities and the Commission relies on external, independent project evaluation and audits.

⁵ Other eligible institutions include the Council of Europe Development Bank (CEB), the Nordic Investment Bank (NIB), Agence Française de Développement (AFD), KfW and Oesterreichische Entwicklungsbank AG (OeEB).

Aside from exploiting the leverage effect (describe earlier) and providing increased concessionality, key aims are to improve donor co-ordination and harmonisation of procedures – hence reducing transaction costs – and improve the ‘visibility’ of joint European operations.

Since May 2008, the NIF Board – chaired by the Commission – has approved grant contributions to projects from the EU budget and the NIF Trust Fund for a total of EUR 277.4 million, EUR 142.6 million of which are allocated to eastern countries and EUR 134.8 million to the southern neighbourhood. Of this total grant contribution, the bulk is from the EU budget, while EUR 36 million is from the Member State funded NIF Trust Fund. For the Eastern window, the majority of the grant funds contributed has been allocated to the EBRD as lead financier (around EUR 100 million).

With total mobilised capital of around EUR 7.3 billion, the leverage effect is estimated to exceed 25x.

2.4 The Investment Facility for Central Asia (IFCA)

The Investment Facility for Central Asia (IFCA) was launched in 2010. Essentially it is a facility that is modelled on the NIF which aims to blend EU budget grant funding with loans by the financial institutions for 5 countries in Central Asia (Kazakhstan, Kyrgyz Republic, Tajikistan, Turkmenistan and Uzbekistan). Unlike the NIF, however, at the present time there are no Member State contributions and so no Trust Fund.

Currently, the IFCA covers projects for the environment and for energy. In the future the sector coverage could be extended to include transport and private sector/SME development.

The initial financial allocation made to the facility in 2010 was for EUR 20 million. A further EUR 45 million is foreseen for the period 2011-2013. So far, as the facility is just starting, just one project has been approved (for EUR 5 million); a joint EIB-EBRD project.

2.5 The Western Balkans Investment Framework (WBIF)

The Western Balkans Investment Framework – a regionally-focused joint grant/lending facility – was launched in December 2009 by the Commission, the EIB, the EBRD and the Council of Europe Development Bank (CEB) (collectively the partner IFIs) as a tool to finance priority projects in the Western Balkans as the countries move closer to potential EU membership. The region is comprised of Albania, Bosnia and Herzegovina, Croatia, the Former Republic of Macedonia, Kosovo (under UNSCR 1244/99), Montenegro and Serbia.

The Framework is an innovative financing initiative which pools grant resources within the Joint Grant Facility (JGF) in order to leverage loans, jointly financed by the partners IFIs collaborating within the Joint Lending Facility (JLF), for the financing of priority infrastructure in the Western Balkans. Eligible sectors include infrastructure development within the environment, energy, transport and social sectors. The scope will expand in 2011 to incorporate regional projects including more than one beneficiary, and the private sector. Available support includes technical assistance, investment co-financing and the provision of interest rate subsidies.

The Fund size is EUR 180 million: EUR 130 million from the Commission, EUR 10 million (each) from the EIB, EBRD and CEB and EUR 25.8 million from bilateral donors to the EWBJF (as at 31 December 2010). The WBIF is summarised in Figure 18.

Figure 18: Key Characteristics of the WBIF

INITIATIVE/PROJECT	THE WESTERN BALKANS INVESTMENT FRAMEWORK
Contribution from the EU	EUR 130 million
Period Covered	To 31 December 2010
Contributions from Others	EUR 10 million (EIB) EUR 10 million (EBRD) EUR 10 million (CEB) EUR 25.8 million (EWBJF)
Programme/Policy Area	Environment/Energy/Transport/Social Expansion in 2011 – regional, involving more than one beneficiary and private sector
Number of Projects supported by WBIF	73
WBIF grants allocated to approved projects	EUR 139 billion
Target IFI resources to be leveraged	>EUR 3 billion
Total project value	>EUR 6 billion

Source: Annual Report 2010, Western Balkans Investment Framework (published for the WBIF Steering Committee on 16 December 2010)

The resources of the JGF originate from:

- a) Grants resources allocated from the EC Instrument for Pre-Accession (IPA)
- b) Grants contributions from CEB, the EBRD and the EIB
- c) Bilateral grant contribution from bilateral donors through the European Western Balkans Joint Fund which is co-managed by the EBRD and the EIB.

As with many of the loan-grant blending instruments described earlier, the provision of technical assistance (TA) plays a key role (see Figure 19). At the first meeting of the WBIF Steering Committee, EUR 25.6 million of grants were allocated for technical assistance support to 26 projects across the region in various sectors (Europa Rapid, 2009).

Figure 19: The Key Role of Technical Assistance

At the [sector level](#), TA can be used to:

- Support **improved policy-making** at the sector level and to **strengthen monitoring and enforcement mechanisms** that ensure their implementation.
- **Improve the definition of investment programmes** at sector level and to **define sustainable cost recovery strategies** for their sustainability.

At [project/promoter level](#), TA can be used to:

- Strengthen the **planning and implementation capacity** of project promoters.
- Improve **project quality** by financing studies or supporting the involvement of relevant stakeholders (eg. final users, particularly poorer communities) in **project design and implementation**.

Source: EC-EIB-IFC Private Sector Workshop, Brussels, 27th January 2010

2.6 The Facility for Euro-Mediterranean Investment and Partnership (FEMIP)

FEMIP was launched back in 2002 and consolidates a range of services that the Commission provides through the EIB to promote the economic development of Mediterranean ‘partner countries’: Algeria, Egypt, Gaza/West Bank, Israel, Jordan, Lebanon, Morocco, Syria and Tunisia. FEMIP has a lending budget of EUR 8.7 billion (for the period 2007-13); resources augmented by loans totally EUR 2 billion under the Euro-Mediterranean Partnership Facility II – as well as EU budgetary funds for technical assistance and private equity activities (EIB, 2010e).

FEMIP makes three main types of product available: loans, private equity and technical assistance. The EIB is currently considering the possibility of providing finance in the form of guarantees. FEMIP products are summarised in Figure 20.

Figure 20: FEMIP Products

Products		Objectives	Beneficiaries
Loan	Lines of credit	To encourage the development of small and medium-sized enterprises by means of lines of credit made available to the EIB's partners – commercial banks or development financing institutions, which then onlend the funds to their own customers.	SMEs
	Individual loans	To develop the economic infrastructure of the Mediterranean partner countries, paying particular attention to the expansion of the private sector and to the creation of a business-friendly environment.	Private and public sector promoters
Private equity		To promote the creation or strengthening of the capital base of productive businesses, particularly those established in partnership with EU-based companies.	<ul style="list-style-type: none"> ↳ Intermediate-sized private enterprises ↳ Investment funds ↳ Microfinance institutions
Technical assistance		To improve the quality of FEMIP operations and their impact on development by: <ul style="list-style-type: none"> ↳ strengthening the capacity of the Mediterranean partner countries and project promoters, ↳ financing studies and activities upstream aimed at consolidating directly and indirectly the expansion of the private sector. 	All FEMIP customers
Guarantees		<ul style="list-style-type: none"> ↳ To stimulate the local capital market ↳ To mobilise additional resources to supplement scarce public capital resources ↳ To support sub-sovereign development ↳ To reduce foreign exchange risk ↳ To reduce government risk exposure 	<ul style="list-style-type: none"> ↳ SMEs ↳ Large corporates ↳ Domestic banks ↳ Public sector promoters ↳ Sub-sovereigns

Source: FEMIP Annual Report 2009, EIB

Between 2002 and 2009, FEMIP:

- Financed 143 projects totalling EUR 10 billion – making it the region's main lender;
- Financed over 1,900 SMEs and helped to create (or save) almost 25,000 jobs;
- Mobilised an additional EUR 25 billion provided by other IFIs, bilateral agencies and the private sector;
- Strengthened its role as a partner for private equity to support SMEs, with a portfolio of over EUR 470 million (involving 535 separate operations);
- Allocated more than EUR 27 million to the microfinance sector;
- Launched 105 technical assistance operations – with a total value of EUR 98.5 million.

In 2009 alone, FEMIP invested EUR 1.6 billion in 20 projects, nearly 70% of which were co-financed with other European and international financing institutions.

2.7 The External Mandate

Although the EIB's primary focus is activity within the EU, a small yet significant proportion (around 10%) of its operations take place outside the EU – amounting to EUR 8.8 billion of projects signed in 2009. The majority of the EIB's 'external financing operations' – supporting EU external policies – benefit from an EU budgetary guarantee (the Community Guarantee). This guarantee is provided by means of a mandate; the so called 'External Mandate' (CEC, 2010d). The EUR 25.8 billion external mandate for 2007-13 covers 79 countries and territories check in the Pre-Accession and Neighbourhood regions, Asia and Latin America – as well as South Africa. Note that EIB activity in the African, Caribbean and Pacific group of states (ACP countries) is covered by a separate ACP-EU Partnership Agreement. This separate agreement is described later.⁶

The Community Guarantee provided by the External Mandate can take the form of a comprehensive guarantee (for sovereign or sub-sovereign sector organisations) or of a political-risk guarantee (for non-sovereign operations). This amounts to cover by the EU budget of country/sovereign risks that the EIB is not currently equipped to take on its own balance sheet (except for investment-grade operations). The External Mandate establishes regional lending ceilings. Exposure of the Community Guarantee is therefore capped by these ceilings. An amount corresponding to 9% of all outstanding liabilities is set aside in a fund (the Guarantee Fund for External Actions). The Guarantee Fund is considered further in Chapter 4 of this report.

The European Parliament required the Commission to conduct, through external evaluation, a mid-term review of the EIB's financing activities outside the EU. This review was completed early in 2010 (Camdessus *et al*, 2010). It concluded that, although EIB operations were in-line with EU external policies, key policy objectives could have been better targeted through a clearer link between the objectives and their operational implementation by the EIB. The review also made a series of generally short-term recommendations about how the EIB's external financing activities could be improved – however these details lie beyond the remit of this report. Of note, however, is the fact that the review recommended the release of a EUR 2 billion optional mandate – that had been held in reserve pending the outcome of the review – specifically in support of initiatives to combat climate change (taking the mandate cap from EUR 25.8 billion to EUR 27.8 billion).

Of specific relevance to this report, the review concluded – in-line with the findings of a working group on blending mechanisms published in December 2009 (CEC-DGECFIN, 2009) – that EU delivery of grant aid should increasingly be delivered through blending mechanisms in circumstances where both grants and loans are required. The report also concluded that co-ordination efforts between IFIs and bilateral financial institutions (BFIs) – and the Commission – should continue to be strengthened. It emphasised that the fight against climate change had become an overarching EU priority, identified the EIB's external mandate (underpinned by the EU guarantee) as being an effective means to serve EU external policies yet suggested that there might be longer-term options to improve external policy attainment through some form of consolidation of the EU's external financing instruments. Importantly, the review encourages the EIB to pursue more own-risk lending, "*taking into account the*

⁶ Aside from lending under the external mandate and that covered by the ACP-EU Partnership Agreement – discussed later – the EIB can lend to non-EU countries at its own risk. The lending ceiling for these own-risk activities was set at EUR 11.2 billion for the period 2007-13; of which EUR 4.9bn (44%) was committed at the end of 2009 (Camdessus *et al*, 2010).

need to preserve the credit standing of the EIB." This issue is considered in more detail elsewhere in this report.

The mid-term review of the EIB's external mandate, its recommendations and subsequent developments represent one important – and dynamic – element of the backdrop of the EU's external cooperation against which this report on EIB and EBRD co-financing has been prepared.

2.8 The ACP Mandate (the ACP-EU 'Cotonou' Partnership Agreement)

Note: The ACP Mandate is included here for completeness. EIB lending in ACP countries – unlike lending under the External Mandate – is guaranteed by the European Development Fund to which Member States contribute. It does not benefit from an EU guarantee and therefore has no EU budgetary implications.

The EIB supports the EU's co-operation and development policies in the African, Caribbean and Pacific regions under the 'Cotonou Partnership Agreement', entered into between the EU and 78 African, Caribbean and Pacific countries. The Agreement, signed in 2000 for a period of 20 years, has three main objectives: sustainable development, the eradication of poverty and integration of ACP countries into the global economy.

The European Development Fund (EDF) is the main instrument for providing Community assistance for development co-operation under the Cotonou Agreement. Funded by Member States, each EDF is concluded for a multi-annual period. The 10th EDF covers the period 2008-13 and has been allocated EUR 22.7 billion. The EDF is complemented by development co-operation funded from the EC budget through the Development Co-operation Instrument, the Instrument for Stability, the European Instrument for Democracy and Human Rights and the European Humanitarian Aid Instrument.

From EDF resources, the EIB currently manages a revolving Investment Facility. This revolving fund supports investments by private and commercially run public sector entities in the ACP regions, including revenue generating economic and technological infrastructure critical for private sector investment. It operates on market related terms with the aim of being financially sustainable over the horizon of the Cotonou Agreement. It comprises a sub-envelope of EUR 400 million grant funding for interest rate subsidies and project-related technical assistance. Investment Facility funds are managed in parallel with a commitment from the EIB to fund projects in ACP countries from its own resources up to EUR 2 billion (see Figure 21).

Figure 21: Mandate under which the EIB Operates

	Funds managed by the EIB	Financial Instruments/Contributors	Budget	Overall budget	Period covered
ACPs	Investment Facility (funded from EDF resources)	• A risk-bearing revolving fund to grant loans, equity and guarantees	3137	3537	2008-2013
		• Interest rate subsidies and technical assistance	400		
	EIB own resources	Senior loans	2000	2000	

Source: European Investment Bank in ACPs and OCTs, Regional Brochure, EIB, November 2008

Note: All figures are EUR million

A second revision to the Cotonou Agreement was signed in June 2010. Notably, this revision allows the EIB to enhance its financing of regional infrastructure projects together with ACP sponsors. It also allows the Bank to accompany South African intermediaries in their drive towards regional economic integration for projects located in the rest of Africa. Since the entry into force of the Cotonou Agreement, around EUR 4.2 billion worth of projects have been signed by the EIB under its Cotonou mandate in ACP countries; more than a third being in the infrastructure sector.

2.9 The Northern Dimension Environmental Partnership

The Northern Dimension Environmental Partnership (NDEP) is a multi-donor fund promoting co-operation between Russia, Belarus, donor governments, the European Union and the International Financial Institutions (IFIs) in order to address urgent environmental problems in the Northern Dimension Area. The purpose of NDEP is to pool funds to make it easier to finance priority projects to help eliminate ecological hot-spots and nuclear safety risks caused by radioactive waste. The concept of NDEP was initially developed under the Finnish Presidency of the European Union and the Partnership was formally established in 2012 when the Rules of the Fund were adopted by the EBRD Board. The EBRD is acting as the Fund Manager of NDEP.

The nuclear window projects are entirely grant funded and administered by the EBRD Nuclear Safety Department. The environmental window projects are developed by the IFIs (EBRD, EIB, NIB and NEFCO) where NDEP grants are used alongside the IFI loans. The grants provide an incentive for beneficiaries to take out IFI loans and also to leverage local funding. NDEP environmental projects focus mainly on improving wastewater treatment, solid waste management and energy efficiency in the municipal sector to maximise environmental benefits and cross-border impacts for all countries in the ND area.

So far the pledges and contributions to NDEP have reached EUR 308 million with a roughly equal split for both windows of the Fund. The Assembly has so far approved EUR 115 million in grants for 23 environmental projects which has helped to leverage EUR 660 million in IFI loans (see Figure 22).

Figure 22: The Northern Dimension Environmental Partnership

INITIATIVE/PROJECT	NDEP
Contribution from the EU	EUR 84 million (EUR 40 million for nuclear safety window and EUR 44 million for environmental window)
Period Covered	2001-2017
Contributions from Others	EUR 224 million from: Russia EUR 40 million France EUR 40 million Canada EUR 20 million Germany EUR 20 million Sweden EUR 26.3 million Finland EUR 18 million United Kingdom EUR 25.2 million Denmark EUR 11 million Norway EUR 12.1 million Netherlands EUR 10 million Belarus EUR 1 million Belgium EUR 0.5 million
Programme/Policy Area	Northern Dimension Area (north-west Russia and northern Belarus)
Proportion Co-Financed by grants for nuclear safety projects	100% for nuclear safety projects 10% for environmental projects

2.10 EBRD-Managed Nuclear Safety Funds

Including the nuclear window of the NDEP, the EBRD manages six donor Funds providing support to enhance nuclear safety. Some 30 donors, including the G-8 countries and the European Commission, have pledged more than EUR 3 billion so far to these Funds. The European Union, which is not only the largest donor with more than EUR 1.5 billion, has also been very active in the inception of these Funds and the implementation of the programs. Four of the six donor Assemblies – the highest decision-making bodies for these Funds – are chaired by representatives of the EC. The EBRD-managed Funds are:

- the Nuclear Safety Account (NSA),
- three international decommissioning support funds for Bulgaria, Lithuania and the Slovak Republic,
- the Chernobyl Shelter Fund (CSF),
- the “Nuclear Window” of the Northern Dimension Environmental Partnership Support Fund (NDEP).

Nuclear Safety Account

Initially, international assistance provided through the EBRD-managed Funds was concentrated on short-term safety upgrades of first generation, Soviet-designed nuclear power plants, with the aim of reducing the risks before their early closure. Today the Nuclear Safety Account funds the construction of a storage facility for spent nuclear fuel from the operation of Chernobyl Nuclear Power Plant.

The closure of Chernobyl Unit 3 in 2000 is an example of the successful outcome of this support. Similarly, Kozloduy Units 1 and 2 in Bulgaria were closed in 2002 and Units 3 and 4 in 2006. Ignalina Unit 1 in Lithuania closed in 2004 and Unit 2 in 2009. Bohunice V1 Units 1 and 2 in the Slovak Republic were closed in 2006 and 2008 respectively.

Decommissioning support

Today the main focus is decommissioning of outdated power plants, for which the necessary infrastructure is typically not in place. The EBRD-managed International Decommissioning Support Funds are used for the construction of spent fuel storage and radioactive waste management facilities, providing for treatment and long-term storage as well as other goods, works and services required to support the decommissioning process.

The decommissioning of power plants is an expensive undertaking. The need to compensate for the resultant loss of electricity generating capacity is an even greater challenge. For this reason the decommissioning funds also support measures in the energy sector and projects to increase energy efficiency, including on the demand side. Examples are co-financing of the Sofia district heating modernisation, energy efficiency projects in the Bulgarian small business and residential sector and the construction of a 450 MW gas fired combined cycle power plant in Lithuania to help compensate for the lost Ignalina generating capacity. Donors have already committed more than EUR 1.5 billion to the three decommissioning funds with the European Community being the biggest contributor by far.

Chernobyl Shelter Fund

In 1986 an accident destroyed Unit 4 of the Ukrainian nuclear power plant Chernobyl. To this date it is one of the major tasks financed through EBRD-managed funds to transform the unit into an environmentally safe state. The CSF-financed Shelter Implementation Plan provides, among other things, for stabilisation of the "sarcophagus" built around the ruins of Unit 4, for a comprehensive monitoring system and for the construction of a new confinement structure to safely enclose the "sarcophagus". According to latest estimates the undertaking will cost more than EUR 1.5 billion.

Northern Dimension Environmental Partnership – Nuclear Window

The NDEP provides grant funding to address severe environmental problems in north-west Russia. NDEP's "Nuclear Window" funds measures to deal with the legacy of the operations of the Russian nuclear fleet in NW Russia, in particular with the resulting spent nuclear fuel and radioactive waste. These measures are needed to control a serious hazard to the environment and to address non-proliferation issues associated with these materials.

The partnership consists of Russia, the European Union, international financial institutions (the EBRD, the Nordic Investment Bank, the European Investment Bank and the World Bank) and donor governments. The EBRD manages the NDEP Support Fund, now at EUR 311 million, which ensures the effective delivery of international support. NDEP deals with water and waste-water treatment, waste and energy efficiency.

2.11 The Eastern Europe Energy Efficiency and Environment Partnership

The Eastern Europe Energy Efficiency and Environment Partnership (E5P) is a newly established multi-donor Fund modelled on NDEP (described earlier). The concept was proposed by Sweden during its Presidency of the European Union in the second half of 2009. The key objectives of E5P are: improvement of energy efficiency, significant reduction of CO₂ and other emissions, enhanced economic competitiveness and affordability of asset maintenance, improvement of pricing policies and secondary regulatory mechanisms in order to have an impact on changed energy consuming behaviour. Based on the NDEP model, the IFIs will develop projects with E5P grants intended to complement loan funding to make the investments financially viable.

Ukraine is the initial focus of the E5P but the Partnership is intended to extend its operation to other Eastern Partnership countries (ie. Armenia, Azerbaijan, Belarus, Georgia and Moldova). The EBRD has been entrusted with the role of the E5P Manager on the same basis as for NDEP. The E5P Fund was formally established in November 2010. The initial pledges to E5P, announced in Stockholm in November 2009, total over EUR 90 million. The IFIs are now preparing a project pipeline and the first SG and Assembly meetings are planned for the first quarter of 2011.

The E5P will have a barrier breaking role both as co-financier for investments and also with regards to regulatory issues for the Ukrainian utility sector which is in considerable need of modernization (see summary in Figure 23).

Figure 23: The Eastern Europe Energy Efficiency and Environment Partnership

INITIATIVE/PROJECT	NDEP
Contribution from the EU	EUR 40 million
Period Covered	2010-2019
Contributions from Others	EUR 50 million from: Denmark EUR 5 million Estonia EUR 0.16 million Finland EUR 2 million Latvia EUR 0.05 million USAID USD 7.5 million Norway EUR 5 million Sweden EUR 24 million Poland EUR 0.194 million Ukraine EUR 10 million
Programme/Policy Area	Ukraine and other countries in the Eastern Partnership
Proportion Co-Financed by grants	Between 100-30%

2.12 Other Initiatives Outside the EU

The main EU/EIB and EU/EBRD joint initiatives in operation outside the EU have been mentioned in the preceding paragraphs. Figure 24 summarises others; mainly smaller or country-specific initiatives (but joint actions nevertheless).

Figure 24: Other Initiatives Outside the EU

INITIATIVE	REGION	FUNDING DETAILS	DESCRIPTION
ACP Water Project Preparation Facility (Water PPF)	ACP	EU contributes EUR 2.25m as grants. EIB contributes EUR 0.75m.	Demand-driven instrument supporting upstream project preparation (inc. Institutional/policy development) to create bankable projects.
Co-Financing EU IPA ISPA 2007-11	Croatia	EU contributes EUR 593m; EIB contributes EUR 200m.	Co-financing under the IPA programme and selected ISPA projects primarily in transport and the environment.
Energy Efficiency Finance Facility (EEFF)	EU & Pre-Accession Countries	EU contributes EUR 25.7m (2006) EUR 13.5 (2007) EBRD loans EUR 100m(2006)	Improving energy efficiency and reducing CO2 emissions. Combines an EIB credit line (and/or risk sharing) with EU funds.

		EUR 60m (2007) EIB contributes > EUR 78m.	
European Fund for South-East Europe (EFSE)	EU & Pre-Accession Countries	EUR 85m (EU). EUR 676m total (EU, MSs, IFIs & BFs).	Loans to micro/small enterprises and private households via financial institutions.
Global Energy Efficiency and Renewable Energy Fund (GEEREF)	Global	EUR 108m (EU, Germany & Norway).	Fund of funds advised by EIB/EIF to provide clean energy to emerging/transitioning economies.
Greater Anatolia SME Loan	Turkey	EU contributes EUR 32m. EIB EUR 250m.	Loan for SMEs in least developed provinces of East Turkey. Credit guarantee provided by EIF.
Green for Growth Fund	Pre-Accession Countries	Shareholders of GGF are the following: KfW, EIB, EBRD, IFC, EIF (as trustee for the EC), KfW (as trustee for BMZ) The EU contribution is EUR 19.6 million in C-shares The EBRD contribution is EUR 25 million: 20.4 million in A-shares and EUR 4.6 million in B-shares.	Energy efficiency fund providing loans and TA to financial intermediaries in SE Europe and Turkey.
IPF Infrastructure Project Facility Municipality Window	Western Balkans	EU contributes EUR 16m. EIB contributes EUR 54m.	TA & financial support to municipal infrastructure projects.
Latin America Investment Facility (LAIF)	Latin America	EU contributes EUR 125m (2009-13). 2010 budget = EUR 35m.	LGB & TA facility.
Municipal Finance Facility (MFF)	EU & Pre-Accession Countries	EU contributes EUR 33m, EIB contributes EUR 348, EBRD contributes EUR 190m	Joint assistance to municipalities in the MSs and candidate counties for infrastructure investment.
Municipal Infrastructure Facility (MIF)	EU & Pre-Accession Countries	EU contributes EUR 40m. EIB contributes EUR 200m.	Joint assistance to border regions in the candidate countries through smaller municipal infrastructure investment.

SME Finance Facility (SME FF)	EU & Pre-Accession Countries	EU contributes EUR 191m, EIB contributes EUR 690m, EBRD contributes EUR 1,350m	Reform and strengthening the financial sector and facilitating SME access to finance.
Western Balkans Private Sector Support Facility	Pre-Accession Countries	EU contributes EUR 31.5m, EBRD contributes loans of EUR 110m	Support for investments in SME competitiveness and sustainable energy
Turkey Private Sector Support Facility	Turkey	EU contributes EUR 22.5m, EBRD contributes loans of EUR 650m. EIB co-financing of circa EUR 225m	Support for MSME (EBRD EUR 150 mn and sustainable energy investment financing (includes TurSEFF programme for small scale EE/RES investments involving EUR 100m EBRD funding and MidSEFF programme for midsize renewables involving EUR 400m EBRD funding and up to EUR 225m EIB co-financing).
Eastern Partnership SME Finance Facility	Eastern Partnership Countries	Newly signed tripartite agreement between EBRD, KfW and EU. EU contributes EUR 10.2 million (from NIF) for technical assistance and credit enhancement support under this Facility	Strengthen confidence and ability of the financial sector to lend to SMEs, promote continued development of market based financial institutions and contribute to institution building, and strengthen and deepen the SME credit markets
SME Recovery Support Loan	Turkey	EU contributes EUR 30m. EIB contributes EUR 120m.	LGB to intermediary banks to provide concessional loans to SMEs in Turkey.

Notes: Shaded instruments are provided by EU & EIB/EIB Group alone. Non-shaded instruments are available to other IFIs. EU contributions are grants; EIB contributions are loans. MSs = Member States. LGB = loan/ grant blending. The 'Northern Dimension Area' covers the Baltic and Barents Seas region.

ANNEX 2 CREDIT RATINGS: DEFINITION

A credit rating is a forward-looking opinion about the creditworthiness of an obligor with respect to a specific financial obligation, a specific class of financial obligations, or a specific financial programme. It takes into consideration the creditworthiness of guarantors, insurers (such as monoline insurers), or other forms of credit enhancement on the obligation and takes into account the currency in which the obligation is denominated. The opinion reflects the credit rating agency's view of the obligor's capacity and willingness to meet its financial commitments as they come due, and may assess terms, such as collateral security and subordination, which could affect ultimate payment in the event of default.

Credit ratings are based, in varying degrees, on the rating agency's analysis of the following considerations:

- Likelihood of payment – capacity and willingness of the obligor to meet its financial commitment on an obligation in accordance with the terms of the obligation;
- Nature and provisions of the obligation;
- Protection afforded by, and relative position of, the obligation in the event of bankruptcy, reorganisation, or other arrangement under the laws of bankruptcy and other laws affecting creditors' rights.

Credit ratings are an assessment of default risk, but may incorporate an assessment of relative seniority or ultimate recovery in the event of default. The following definitions apply (adapted from Standard & Poor's, August 2010):

AAA

An obligation rated 'AAA' has the highest credit rating. The obligor's capacity to meet its financial commitment on the obligation is extremely strong.

AA

An obligation rated 'AA' differs from the highest-rated obligations only to a small degree. The obligor's capacity to meet its financial commitment on the obligation is still very strong.

A

An obligation rated 'A' is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than obligations in higher-rated categories. However, the obligor's capacity to meet its financial commitment on the obligation remains strong.

BBB

An obligation rated 'BBB' exhibits adequate protection parameters. However, adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity of the obligor to meet its financial commitment on the obligation

BB, B, CCC, CC & C

Obligations rated 'BB', 'B', 'CCC', 'CC', and 'C' are regarded as having significant speculative characteristics. 'BB' indicates the least degree of speculation and 'C' the highest. While such obligations will likely have some quality and protective characteristics, these may be outweighed by large uncertainties or major exposures to adverse conditions.

BB

An obligation rated 'BB' is less vulnerable to non-payment than other speculative issues. However, it faces major ongoing uncertainties or exposure to adverse business, financial, or economic conditions which could lead to the obligor's inadequate capacity to meet its financial commitment on the obligation.

B

An obligation rated 'B' is more vulnerable to non-payment than obligations rated 'BB', but the obligor currently has the capacity to meet its financial commitment on the obligation. Adverse business, financial, or economic conditions will likely impair the obligor's capacity or willingness to meet its financial commitment on the obligation.

CCC

An obligation rated 'CCC' is currently vulnerable to non-payment, and is dependent upon favourable business, financial, and economic conditions for the obligor to meet its financial commitment on the obligation. In the event of adverse business, financial, or economic conditions, the obligor is not likely to have the capacity to meet its financial commitment on the obligation.

CC

An obligation rated 'CC' is currently highly vulnerable to non-payment.

C

A 'C' rating is assigned to obligations that are currently highly vulnerable to non-payment, obligations that have payment arrears allowed by the terms of the documents, or obligations of an issuer that is the subject of a bankruptcy petition or similar action which have not experienced a payment default. Among others, the 'C' rating may be assigned to subordinated debt, preferred stock or other obligations on which cash payments have been suspended in accordance with the instrument's terms or when preferred stock is the subject of a distressed exchange offer, whereby some or all of the issue is either repurchased for an amount of cash or replaced by other instruments having a total value that is less than par.

D

An obligation rated 'D' is in payment default. The 'D' rating category is used when payments on an obligation, including a regulatory capital instrument, are not made on the date due even if the applicable grace period has not expired, unless the rating agency believes that such payments will be made during such grace period. The 'D' rating also will be used upon the filing of a bankruptcy petition or the taking of similar action if payments on an obligation are jeopardised. An obligation's rating is lowered to 'D' upon completion of a distressed exchange offer, whereby some or all of the issue is either repurchased for an amount of cash or replaced by other instruments having a total value that is less than par.

Plus (+) or minus (-)

The ratings from 'AA' to 'CCC' may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the major rating categories.

ANNEX 3 LIST OF INTERVIEWEES

Interviewees: EIB

Tom Barrett	Director – New Products and Special Transactions (Operations inside the EU): OPS A
Birthe Bruhn-Leon	Head of Mandate Management, European Investment Fund: EIF
Alessandro Carano	Head of Unit for Institutional and Operational Policies outside the EU (General Secretariat): SG-JU/IAD
Catherine Collin	Head of Division for Portfolio Management & Policy (Operations outside the EU): OPS B
Dominique Courbin	Head of the Western Balkans Division (Operations inside the EU): OPS A
Dominique de Crayencour	Director of the Institutional Affairs Department (General Secretariat): SG-JU/IAD
Dietmar Dumlich	Head of Division for Planning and Co-ordination (Operations inside the EU): OPS A
Janette Foster	Head of Division for Budget, Analysis and Partnership – Strategy and Corporate Centre: SCC
Massimo Galoppo	Deputy Head of Division for Budget, Analysis and Partnership – Strategy and Corporate Centre: SCC
Hugh Goldsmith	Head of Division for Project Development and Implementation Support (Projects Directorate): PJ
Alfredo Panarella	Head of Unit for Institutional and Operational Policies inside the EU (General Secretariat): SG-JU/IAD
Eefje Schmid	Co-ordination Officer – Institutional & Policy Unit (Operations outside the EU): OPS B
Mark Schublin	Director – Mandate Management, Product Development and Incubation – European Investment Fund: EIF
Bernard Ziller	Head of Unit for Policy-Reporting and Information Systems (Operations outside the EU): OPS B

Interviewees: EBRD

Alexander Auboeck	Corporate Director
Mandeep Bains	Senior Manager, Official Co-Financing Unit
Sue Barrett	Director, Transport
Andreas Biermann	Principle Policy Manager, Energy Efficiency & Climate Change
Teresa Goodwin-Coombs	Senior Manager, Financial Institutions/Small Business Finance
Richard Jones	Director, Official Co-Financing Unit
Alexander Lehmann	Senior Economist, Country Strategy and Policy
Thomas Maier	Managing Director, Infrastructure Banking and Front Office
Jean-Paul Marquet	Director, Municipal and Environmental Infrastructure
Franziska Ohnsorge	Senior Economist, Office of the Chief Economist
Claudio Viezzoli	Director, Western Balkans

Interviewees: European Commission

Dirk Ahner	Director General; Deputy Director General – Development, Coordination and Communication of Cohesion Policy
Stefan Appel	Head of Sector, Coordination with IFIs, Coordination with the EIB Group, EBRD and IFIs, DG Economic and Financial Affairs.
Eduardo Barreto	Principal Administrator, Interventions in Romania, DG Regional Policy
Grazyna Bogusz	Programme Manager for Economic and Trade Co-operation, DG Development and Cooperation - EuropeAid
Giorgio Chiarion-Casoni	Head of Unit, Coordination with the EIB Group, EBRD and IFIs, DG Economic and Financial Affairs
Merete Clausen	Deputy Head of Unit, Liaison with the EIB Group and IFIs; New Financial Instruments, DG Economic and Financial Affairs
Antonella Colavita	International Relations Officer - Officer in charge of relations with the World Bank (WB) and International Financing Institutions (IFIs).
Jorge de la Caballeria	Head of Unit, Multi-Country Programmes, DG Development and Cooperation - EuropeAid
Torsten Ewerbeck	Programme Manager- EU Policies, Multi-country Programmes, DG EuropeAid

Conrad Ganslandt	Policy Officer, Financial Engineering, DG Research and Innovation
Christos Gofas	Head of Section, Economic Development and IFI Cooperation, Regional Programmes, DG Enlargement
Roger Havenith	Deputy Head of Unit, Financing of Innovation, Competitiveness and Employment Policies, DG Economic and Financial Affairs
Jeremy Heath	Financing Innovation and SMEs, DG Enterprise and Industry
Dr. Karl Kellner	New and Renewable Sources of Energy, Energy Efficiency and Innovation, DG Energy
Florence Leroy	International Relations Officer, International Energy Relations and Enlargement, DG Energy.
Milosz Momot	Programme Manager, Unit B1 – Energy Policy, Security of Supply and Networks, DG Energy
Stephane Ouaki	Policy Officer, Trans-European Transport Network Policy, Research Coordination and European Radio Navigation Plan, DG Mobility and Transport
Jesper Pedersen	Head of Sector – Economics; Private Sector Development and Trade Related Assistance; Centralised Operations – Africa, Caribbean and the Pacific, DG EuropeAid
Carsten Rasmussen	Deputy Head of Unit, Bulgaria, DG Regional Policy
Jean-Marie Seyler	Director, Interventions in Bulgaria, Cyprus, Greece, Hungary and Romania; IPA/ISPA Accession Negotiations, DG Regional Policy
Gerassimos Thomas	Director, Finance Coordination with EIB group, EBRD and IFIs, DG Economic and Financial Affairs.
Eleftherios Tsiavos	Head of Section, Natural Resources and Infrastructure, Centralised Operations for the ACP Countries, DG EuropeAid
Dorota Kalina Zaliwska	Head of Unit, Financial Engineering, Major Projects, DG Regional Policy

Interviewees: The European Court of Auditors

Olavi Ala-Nissilä	Member, Chamber I (Preservation and Management of Natural Resources)
Vitor Caldeira	President, European Court of Auditors
Turo Hentilä	Head of Cabinet of Mr Ala-Nissilä
Igors Ludboržs	Member of the European Court of Auditors

Gaston Moonen

Head of Private Office of Mr Igors Ludboržs

Bernard Moya

Attaché, Private Office of Mr Igors Ludboržs

Staff at the European Commission, EBRD and EIB were incredibly accommodating and helpful; making themselves available to answer questions, to be interviewed and for follow-up enquiries. We are very grateful to them all. In addition, there are some particular individuals who went to great efforts to provide extra assistance to us. In that context, we would especially like to acknowledge the help of Mandeep Bains (EBRD, London), Patrick Steimer (EC, Brussels) and Laurence de Vos, Alessandro Carano and Hugh Goldsmith (all EIB, Brussels & Luxembourg). Any errors in the report are, of course, the responsibility of the authors alone.

ANNEX 4 SEMI-STRUCTURED INTERVIEW 'PROMPT SHEET'

The Implications of EIB (and EBRD) Co-Financing for the EU Budget

- Please describe your role today in relation to Bank operations that benefit from EU funds, co-financing and/or participation.
 - How has EU participation evolved in the past?
 - How has this been impacted by the Global Financial Crisis?
 - How do you think it might develop in the future?
- Do you feel that EU and EIB policy objectives are perfectly aligned?
 - If yes/no, please give examples.
 - How does this work in practice?
- Are you involved with or aware of Bank products/initiatives that are guaranteed by the EU (eg. in the event of loan default)?
 - Please describe.
 - Has the EU guarantee ever been called?
- We would also like to discuss the area of governance, control, transparency, visibility etc. and the extent to which that is effected by the growth of co-financing.
 - Are the instruments currently in place sufficient?
- Finally, on the external mandate.
 - How effective are the synergies with blending EU grants and EIB loans?
 - How does the process work in relation to EIB, EBRD and EU collaboration?
- Are there any documents or reports which you are aware of that could be useful to our research?
 - Could somebody forward those to us?

Study contact people:

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Thank you

ANNEX 5 INFORMATION FOR INTERVIEWEES

The Implications of EIB (and EBRD) Co-Financing for the EU Budget

- This study has been commissioned by the European Parliament's Committee on Budgets. The study is examining EIB-managed operations that receive funds from the EU budget, EIB lending guaranteed by the EU and other EIB activities or programmes that benefit from EU contributions (eg. grants).
- As part of the study, semi-structured interviews are being conducted with EIB staff who are involved in EU-related (or financed) initiatives. Your name has been put forward in that context.
- The interviews are being conducted by Nick Robinson (from the UK's University of Leeds) and Robert Bain (an independent consultant who has previously worked for the EIB).
- The interviews will last approximately one hour. There is no need for any formal preparation – although we would appreciate follow-up if appropriate (eg. forwarding to us any documents identified during the interview that might contribute to the study).
- The interviews will be recorded however this is for [our benefit only](#). Individuals' views and comments will remain anonymous in our report to the Committee. As we are particularly keen to hear frank and open opinions, the recording will be switched off at the interviewee's request (for any 'off the record' remarks).
- For more information about the study or the study team, please contact:

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